



STATE OF TENNESSEE
DEPARTMENT OF FINANCE AND ADMINISTRATION
INSURANCE ADMINISTRATION
1300 William R. Snodgrass Tennessee Tower
312 Eighth Avenue North
Nashville, TN 37243

August 31, 2007

Ladies and Gentlemen:

We are pleased to submit the 2006 Annual Program and Financial Report of the Division of Insurance Administration. This unit of the Department of Finance and Administration manages insurance benefits for over 139,000 employees of and over 21,000 medicare eligible retirees from public sector organizations in Tennessee. At the end of 2006, the state-sponsored plans provided health insurance coverage to over 267,000 individuals.

The data presented here demonstrates trends from program, statistical and financial standpoints. The financial statements reflect the fiscal year ended June 30, 2006.

During 2006, several developments were noteworthy.

- For the first time, on a combined basis, the State, Local Education and Local Government Plans provided over \$1 billion in benefits to plan members.
- Administrative costs for the medical options were less than 5 percent of plan expenses.
- Just under 1 percent of plan participants received benefit payments in excess of \$50,000 during 2006. The group received 20 percent of plan payments; the average payment to this group was \$99,247. Without the participation of the 45 percent of plan members who did not require medical treatment but made premium payments, the public sector plans could not provide affordable coverage, access to medical care and the financial security the Plans provide.

As noted in the Opportunities section, the division initiated development and implementation of Cover Tennessee, an initiative of State Government to expand the availability of health insurance to uninsured Tennesseans. Coverage was first available during the spring of 2007.

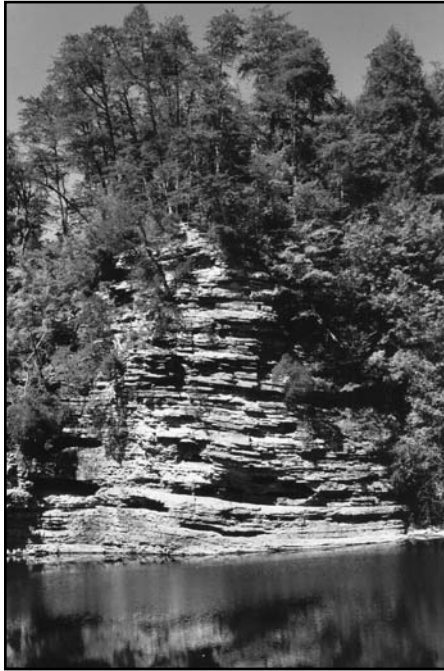
The division also continued its efforts, begun in 2005, to assess the business and software capability of the replacement of the Plan's eligibility and enrollment mainframe system. The state's new business software, known as Edison, will replace the legacy system at the beginning of 2008 resulting in significant changes in both business processes and customer service practices.

While the state group insurance program sponsors the coverages and programs reviewed in this report, we work in partnership with 12 contractors and a number of other state agencies to deliver services to program participants. The results reported here reflect their contribution, as well.

Sincerely,

Richard Chapman, Executive Director

M. D. Goetz Jr., Commissioner



COVER PHOTO
Cane Creek
Fall Creek Falls State Park

PHOTO CREDIT
Dennis Minton

5 INTRODUCTION

13 PROGRAM AND STATISTICAL INFORMATION

31 FINANCIAL STATEMENTS



Tennessee Department of Finance and Administration. Authorization Number 317238, 1,000 copies, June 2007.
This public document was promulgated at a cost of \$3.05 per copy.

INTRODUCTION

Overview

The Division of Insurance Administration operates within the State of Tennessee's Department of Finance and Administration. A committed staff of 40 works to administer health, dental, life and long-term care insurance coverages for over 292,000 public sector employees, retirees and their covered dependents.

In addition to insurance coverages, the division also administers an employee assistance program and a state employee wellness program. These related programs complement insurance programs by educating employees and their families about prevention and behaviors that can affect their physical and mental health.

State group insurance program participants include state government and higher education employees, as well as employees of local school systems and local government agencies who elect to participate in one of the state-sponsored plans. Various quasi-governmental and nonprofit agencies receiving state support may also elect to participate in the local government plan.

Enrollment Highlights

| | |
|----------------------------------|---------|
| Total Group Health Lives | 267,966 |
| Employees: | |
| State PPO | 29,140 |
| State POSs | 22,791 |
| State HMOs | 23,934 |
| Local Education PPO | 24,115 |
| Local Education POSs | 18,953 |
| Local Education HMOs | 7,861 |
| Local Government PPO | 3,916 |
| Local Government POSs | 5,519 |
| Local Government HMOs | 2,774 |
| Local Government PPO Limited | 693 |
| Total Employee Group Health | 139,696 |
| Optional Dental Coverage | 44,821 |
| Optional Life Insurance Products | 68,323 |
| Optional Long-Term Care Coverage | 2,491 |
| Retiree Medicare Supplement | 21,923 |

The preferred provider organization (PPO), administered through BlueCross BlueShield of Tennessee, is available statewide to all participants.

A point of service (POS) option is also available statewide. POS offerings in 2006 were administered by Cigna Healthcare in all service areas.



Health maintenance organizations (HMOs) are offered in 72 of Tennessee's 95 counties. HMO offerings in 2006 were: Cigna Healthcare Memphis, Cigna Healthcare Nashville, United Healthcare Chattanooga, United Healthcare Knoxville and United Healthcare Tri-Cities.



In addition to health insurance, participants in all three plans may enroll in optional dental coverage choosing either the preferred provider plan administered by Delta Dental of Tennessee or the prepaid plan administered by Assurant Employee Benefits.

State employees are provided basic term life and accidental death and dismemberment coverage through Fort Dearborn Life while the optional term and universal life coverages are underwritten by Unum Group.

Long-term care insurance is available to state employees, retirees and eligible family members through MedAmerica Insurance Company.

Governance

The authorization for providing group insurance benefits for public officers, state, local education and local government employees and retirees is found in Chapter 27 of Title 8, Tennessee Code Annotated.

The benefit plans authorized by this legislation are governed separately by three committees identified as the State, Local Education and Local Government Insurance Committees. Each of these committees represents the interests of the employer(s) and their employees and retirees in financially separate benefit plans.

The responsibilities of each committee can be summarized under four broad areas:

- 1) To establish the benefit plans offered.
- 2) To approve premiums necessary to fund plan operations.
- 3) To provide for the administration of certain plan functions through the selection of contractors and monitoring of vendor performance.
- 4) To establish and review policy related to eligibility, benefits and appeals.

Committee Members

M. D. Goetz Jr., Chairman — S, E, G
Commissioner, Department of Finance and Administration

John G. Morgan — S, E, G
Comptroller of the Treasury

Dale Sims — S, E, G
State Treasurer

Paula Flowers — S, E
Commissioner, Department of Commerce and Insurance

Deborah Story — S
Commissioner, Department of Personnel

Jeannie Bellephant — S
Employee Representative

Tom Spillman — S
Employee Representative

Charles Peccolo — S
Higher Education Representative

Jim Tucker — S
Tennessee State Employee Association

Elfreda Tyler — E
Designee, Department of Education

Donna Barber — E
Middle Tennessee Teacher Representative

Clark Justis — E
East Tennessee Teacher Representative

Cindy Lumpkin — E
West Tennessee Teacher Representative

Phillip White — E
Tennessee School Boards Association

Tommy Pedigo — G
Tennessee Municipal League

Bob Wormsley — G
Tennessee County Services Association

S — State Insurance Committee
E — Local Education Insurance Committee
G — Local Government Insurance Committee

Contract Partners

The division works in partnership with the following entities in the administration of insurance benefits and related administrative functions:

BlueCross BlueShield of Tennessee

Providing for administration of healthcare coverage for plan members in the preferred provider organization (PPO), high-risk PPO limited and retiree medicare supplement programs.

United Healthcare

Providing for administration of healthcare coverage for plan members in the health maintenance organization (HMO) east.

Cigna Healthcare

Providing for administration of healthcare coverage for plan members in the point of service (POS) in all service areas and the health maintenance organization (HMO) Memphis and Nashville.

Fort Dearborn Life Insurance Company

Providing basic term and accidental death and dismemberment insurance for state plan members enrolled in a healthcare option and medical underwriting services for those applying for coverage as late applicants.

Unum Group

Providing optional term and universal life insurance to state plan members who choose to enroll in this coverage.

Assurant Employee Benefits

Providing optional prepaid dental insurance to participating plan members statewide.

Delta Dental of Tennessee

Providing optional preferred provider dental insurance to participating plan members statewide.

Magellan Health Services

Providing employee assistance program (EAP) services and administration of mental health and substance abuse coverage for plan members.

MedAmerica Insurance Company

Providing long-term care coverage to state plan members and their eligible family members who choose to enroll in this coverage.

Harris Health Trends

Providing support for wellness program services for central state plan members enrolled in a healthcare option.

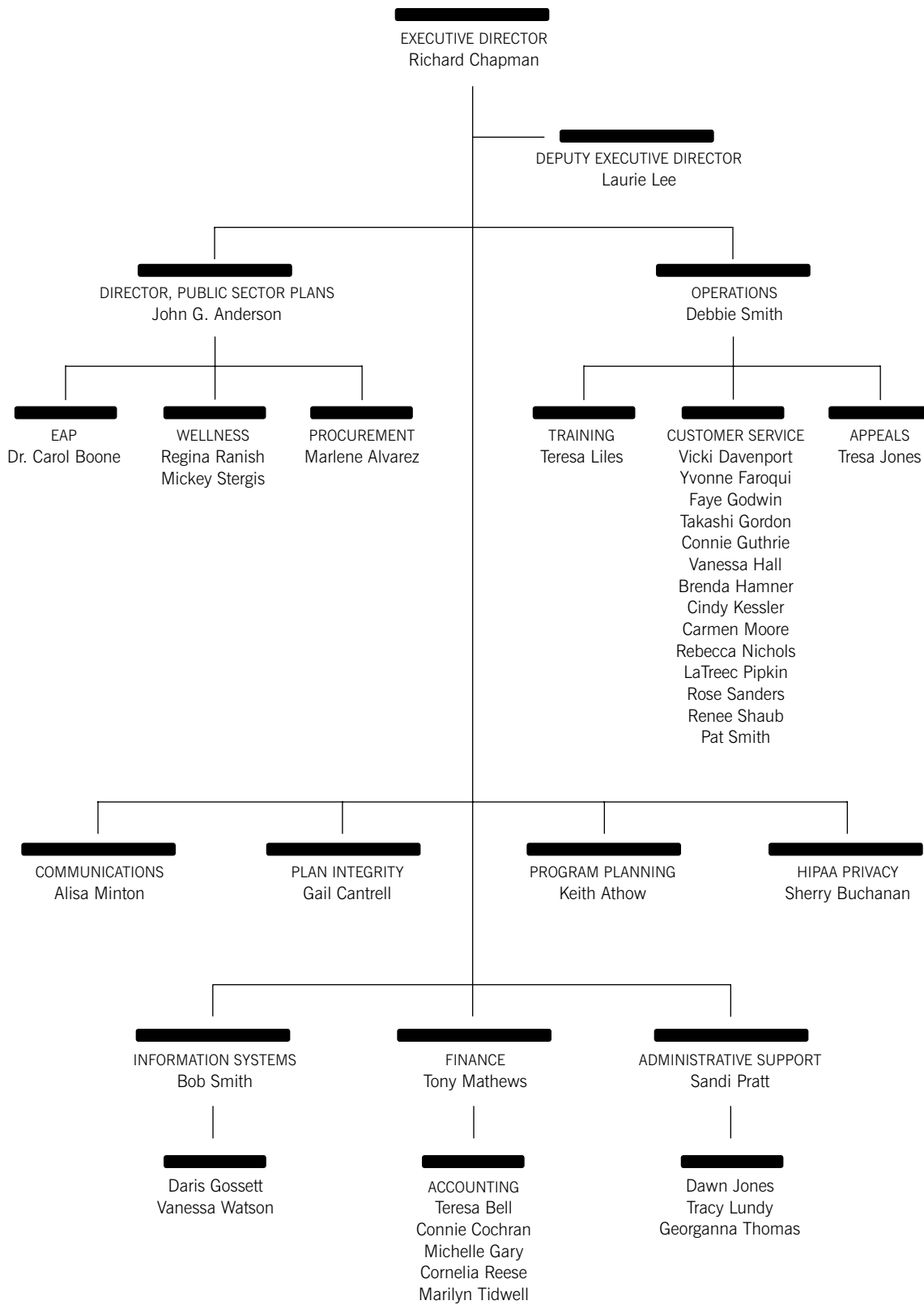
The Medstat Group

Providing analytical services to assess healthcare utilization and claims-based cost for our population.

Buck Consultants

Providing benefits and administrative consultant services to the division.

Organization



Accomplishments

The division initiated and completed three competitive procurements through the state's request for proposals (RFP) process. Services procured for 2007 resulted in a change from BlueCross BlueShield of Tennessee to the POMCO Group as the claims administrator for the state-sponsored retiree Medicare supplement plan. Based on the lower administrative costs, this procurement resulted in a 15 percent premium decrease for plan members effective 2007. The RFP for the state-sponsored PPO healthcare option resulted in the re-selection of BlueCross BlueShield of Tennessee as the claims administrator. Harris Health Trends will continue as the provider for specialized services associated with the state employee wellness program.

Due to the Medicare Modernization Act, which authorized the new Medicare Part D prescription drug coverage, the Medicare supplement policies offered by the state group insurance program no longer provide for a pharmacy benefit. The membership of Plan One, Plan Two and Plan Three were consolidated into a single plan — The Tennessee Plan. Premiums were modified accordingly.

Responding to the requirements of the "State of Tennessee Audit Committee Act of 2005," the Insurance Committees established an Audit Committee consisting of three plan members. The primary purpose of the Audit Committee will be to assist the Insurance Committees in fulfilling their oversight responsibilities with respect to:

- The financial reporting process
- The system of internal controls and risk management
- The internal and external audit process

The Audit Committee will work closely with the staff of the division to ensure that adequate policies and procedures are in place in order to protect against fraud, waste and abuse.

Based on action by the general assembly, the state support for medicare eligible retired state employees and retired public school teachers was increased. The new service-based contribution is \$50 per month for those with 30 or more years of service, \$37.50 for those with 20-29 years of service and \$25 for those with 15-19 years of service. The change became effective in August.

The appeals process established by the Insurance Committees received 244 requests for a benefits review; 125 were resolved by the division appeals coordinator without the need for a formal

written appeal. The remaining 119 filed a formal written appeal with 84 cases resolved during initial review between the division and the claims administrator. Of the 23 cases reviewed by the Staff Appeals Committee, 10 were approved, 12 denied and 1 deferred. The remaining 12 cases were still pending decisions at the end of the year.

The division continues to expand the information provided on our web site to allow participants ease of access to information, forms and publications. Over 310,000 publications and forms were downloaded from the site during the year.

A total of 646 individuals applied for coverage through the medical underwriting or proof of insurability process. Of those, 470 were approved and authorized to enroll in coverage.

The division acted on 55 requests for a waiver of life insurance premium due to disability with 28 requests approved and 8 denied. The remaining requests were pending at year end.

During 2006, premium quotes were requested from 42 agencies interested in joining the local government plan. Of those, 21 agencies joined the plan.

The division's eligibility team reviewed 23 cases. Of these, 18 were approved and 5 denied.

Twenty-seven insurance preparer training classes and nine annual transfer meetings were held across the state.

The State Employee Wellness program launched an online wellness calendar called Small Steps to Success to a demonstration group of 4,123 with very positive results. Tip of the Week health information was received by 6,500 employees weekly.

The Employee Assistance Program held its 14th annual March EAP Awareness Month with continuous increased participation from employees. All segments of the employee plan groups participated — State, Local Education and Local Government. This has proven to be a very effective way to promote the services provided by the EAP.

The Employee Assistance Program's initiation of telephonic anonymous self-screening for depression and alcohol use concerns is being utilized successfully by employees.

Opportunities

The contract for benefits consultant services expires December 31, 2007, and the division will issue requests for proposals in order to re-procure these services. These consultant services provide the division with additional expertise in some of the more specialized and complex areas of benefits administration.

The division, in partnership with the Division of Accounts, will secure the services of an actuarial firm to conduct the second assessment of the cost of other post employment benefits (OPEB) required under the Governmental Accounting Standards Board (GASB) rules. This second determination will, in addition to estimating the state's liability, identify the OPEB liability for Local Education Agencies as well as certain Local Government Agencies.

The Audit Committee will continue to carry out their responsibilities as contained in their charter as approved by the Insurance Committees. Specifically during the year they will review the plan funds financial statements, plan annual audits, and division internal controls.

The division will, through the benefits consultant, conduct a pharmacy rebate audit of Caremark the pharmacy benefit manager for BlueCross and BlueShield of Tennessee (BCBST). This audit is intended to determine if the plans administered by BCBST are properly receiving all the pharmacy rebates they are entitled to.

The state will continue to participate in the procurement and implementation of the state's Edison project, which represents a significant opportunity to upgrade the division's 15 year old eligibility, enrollment and premium collection software. The division will work closely with Edison staff in review of proposals and the design and functionality of the insurance module. Edison is scheduled to "go live" on January 1, 2008.

The Employee Assistance Program will promote participation in its supervisory training module to educate supervisors of its use for aiding troubled employees and will enhance utilization of expanded services such as legal and financial assistance through increased media coverage.

New Initiative — Cover Tennessee

In 2006, Governor Phil Bredesen announced a new initiative to provide health coverage options for uninsured Tennesseans. The program, called Cover Tennessee, is administered by the Division of Insurance Administration and extends coverage to uninsured children, chronically ill adults and uninsured working Tennesseans. These programs are not part of the public sector plans provided by the state group insurance program.

- AccessTN is a comprehensive health insurance plan for seriously ill adults who are uninsurable due to an existing medical condition. There is no income determination to apply and premium assistance is available to those individuals with a household income below 250 percent of the federal poverty level. Individuals cannot have access to insurance at the time of application and there is a requirement that applicants may not have had insurance coverage during the past six months.
- CoverKids offers comprehensive health coverage to low income, uninsured children in Tennessee, age 18 and under, and pregnant women. It is a State Children's Health Insurance Program (SCHIP), which is a partnership between the federal and state governments. In accordance with federal guidelines, CoverKids applicants must first be screened for eligibility for TennCare and to determine if they have access or are enrolled in a State Health Benefit plan due to a parent or guardian's employment. Additionally, the child may not have had insurance coverage during the past three months to qualify.
- CoverRx offers access to affordable medications to low income Tennesseans who do not have prescription drug coverage. This includes TennCare, Medicare or employer-sponsored drug coverage. Participants do not pay a monthly premium to participate, but copayments are required for prescriptions based on income guidelines.

- CoverTN partners the state, private employers and individuals to offer guaranteed affordable basic health coverage for employees of Tennessee's small businesses. Businesses with 25 or fewer full-time employees within a designated median wage may apply for approval to offer this coverage. There is also a requirement that the business may not have offered health coverage to employees within the past six months for which they paid at least 50 percent of the monthly premium.

Building on its experience in the design, development and operation of insurance coverages for public sector employees, the Division of Insurance Administration took the following steps to implement Cover Tennessee:

- Provided extensive testimony to the General Assembly during the consideration of the enabling legislation for CoverTN, CoverKids and AccessTN.
- Finalized estimates of enrollment and budgetary requirements for each of the Cover Tennessee components.
- Recruited 21 new staff members to guide development of the coverage options authorized in the enabling legislation.
- Conducted 14 procurements for plan administration, enrollment determination, outreach and marketing and consulting services associated with Cover Tennessee.
- Completed the CoverKids State Plan, the application for federal support through Title 21 of the Social Security Act. The plan was approved by the Centers for Medicare and Medicaid Services in early 2007.
- Submitted a grant application to the Center for Medicare and Medicaid Services to help finance the development of AccessTN. A \$1 million award was announced in September.

PROGRAM AND STATISTICAL INFORMATION

State Plan

State employees, University of Tennessee and Board of Regents employees comprise the state plan. This plan provided coverage for 75,865 active employees, COBRA participants and qualified retirees.

For 2006, the portion of plan members selecting the POS option continued to increase, growing from 21,960 to 22,791. HMO selection increased from 22,710 to 23,934 and PPO participation declined from 30,309 to 29,140.

Employees may choose to participate in optional dental insurance. One prepaid dental plan and one preferred provider dental plan were available. State employees electing dental coverage totaled 36,285 at year end, an increase of 1,110 during the calendar year.

During 2006, Fort Dearborn received over \$9.5 million in premium for the basic term life and the accidental death and dismemberment coverages. Expenses reported for 2006 included \$8.3 million in basic term and accidental death and dismemberment claims and \$631,714 in optional accidental death and dismemberment claims. Administrative fees were \$53,712, reserving requirements were \$433,546, conversion expenses were \$76,088 and taxes were \$117,035.

Employee term life benefits exceeded \$5.9 million and were paid on behalf of 165 employees who died during 2006. An additional \$1.8 million in employee accidental death and dismemberment benefits were provided by the plan. Employees received \$468,064 in benefit payments due to the death of a covered dependent and \$666,858 due to an accident involving the death or dismemberment of a dependent.

At 2006 year end, 14,379 employees were covered under the optional term life insurance plan, in addition to 6,354 spouses and 7,478 children. The coverage for employees exceeded \$1.1 billion, spouse coverage was just over \$133 million and the child term rider amount was \$29 million. Premiums for 2006 were just under \$5 million, while claims totaled \$3.9 million.

The optional universal life covered 7,160 employees and 1,457 spouses who maintained over \$345 million in coverage. About \$5 million of the annual premium paid for the life benefit with

annual claims of \$4 million. At the end of December, the employee cash value had grown to more than \$68 million.

Optional long-term care insurance covered 2,491 individuals at year end. Total premium payment exceeded \$2 million while claims payments totaled over \$128,000 paid on behalf of ten enrollees.

As has been the case for the past several years, benefit payments by the state plan increased again in 2006. For the PPO, total allowed amounts per member increased 12 percent to \$5,826. Inpatient benefits increased by 0.5 percent while outpatient costs grew by 12 percent.

Total allowed amounts per member for the POS increased 12 percent to \$4,266. Inpatient payments increased 18 percent due to a combination of an increase in the number of total inpatient days per 1,000 members and the number of admissions per 1,000 members. Payments for outpatient services rose by 23 percent.

For the PPO, pharmacy plan benefit payments were \$1,410 per member — an 18.9 percent increase over 2005. For the POS, pharmacy payments were \$823 per member — an 18.9 percent increase over 2005.

The state plan paid 87 percent of the eligible PPO expenses and 92 percent of the POS eligible expenses during 2006 while the remaining 13 and 8 percent, respectively, were paid by the plan member. The benefits paid by the HMO were 93 percent of eligible expenses — 1 percent more than in 2005.

The increasing price and utilization of medical services (especially in the outpatient setting) and prescription drugs will continue to have impact on the future increase in plan benefits. Demographic changes, including the aging of the active workforce and the growth in the number of retirees, will also place demands on the future growth of plan costs.

The state continues to monitor its plan benefits each year, with the goal of providing maximum value to plan members while sharing benefit expenses appropriately.

Health Contracts

Preferred Provider Organization (PPO)

| | |
|----------------------|--------|
| BlueCross BlueShield | 29,140 |
| Percent of Total | 38.4% |

Health Maintenance Organization (HMO)

| | |
|---------------------------------|-------|
| Nashville — Cigna Healthcare | 8,172 |
| Percent of Total | 10.8% |
| Memphis — Cigna Healthcare | 4,189 |
| Percent of Total | 5.5% |
| Knoxville — United Healthcare | 5,860 |
| Percent of Total | 7.7% |
| Chattanooga — United Healthcare | 2,567 |
| Percent of Total | 3.4% |
| Tri-Cities — United Healthcare | 3,146 |
| Percent of Total | 4.1% |

Point of Service (POS)

| | |
|---------------------------|--------|
| West — Cigna Healthcare | 7,118 |
| Percent of Total | 9.4% |
| Middle — Cigna Healthcare | 12,182 |
| Percent of Total | 16.1% |
| East — Cigna Healthcare | 3,491 |
| Percent of Total | 4.6% |

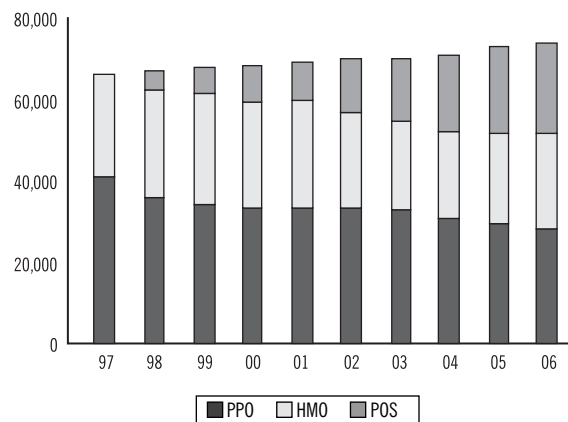
Optional Insurance Contracts

| | DEC. 31, 2006 | DEC. 31, 2005 |
|--------------------------------|---------------|---------------|
| Dental Insurance | | |
| Prepaid Plan | 20,750 | 20,579 |
| Preferred Provider Plan | 15,535 | 14,596 |
| Total Dental | 36,285 | 35,175 |
| Optional Life Coverages | | |
| Term Life | 28,211 | 27,232 |
| Universal Life | 8,617 | 8,687 |
| Special Accident | 30,882 | 30,992 |
| Perma Plan | 613 | 706 |
| Total Life | 68,323 | 67,617 |

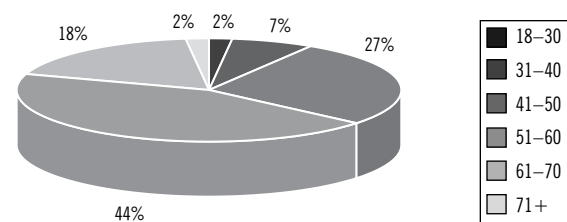
Long-Term Care Insurance

| | | |
|-------------------------|-------|-------|
| Employees | 1,897 | 1,887 |
| Retirees | 80 | 81 |
| Eligible Family Members | 514 | 509 |
| Total Long-Term Care | 2,491 | 2,477 |

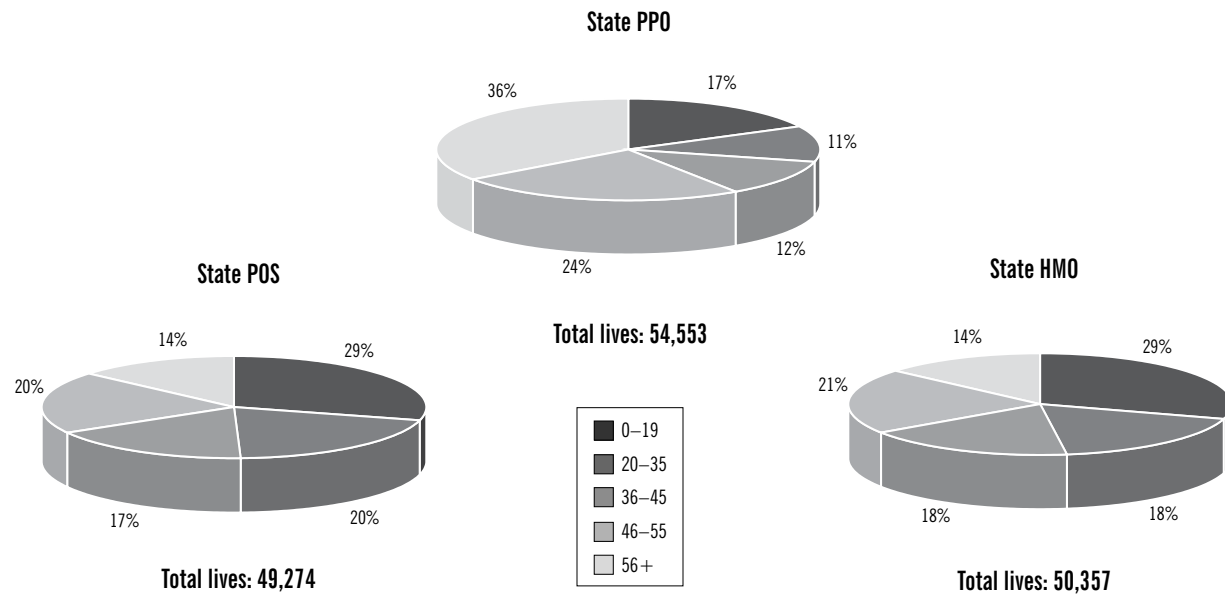
Total Contracts by Healthcare Option



Long-Term Care Enrollment Demographics



Health Enrollment Demographics



Chronic Conditions—Patients and Medical Costs

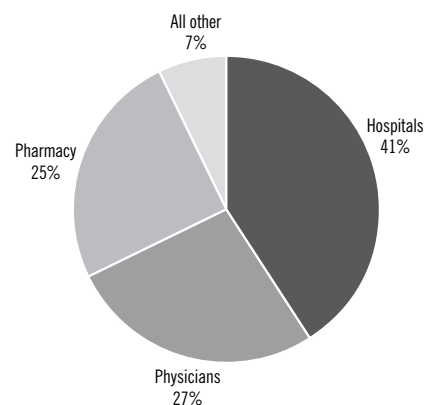
| | TOTAL PATIENTS | TOTAL COSTS |
|--------------------------------|----------------|---------------|
| Hypertension | 26,915 | \$ 5,004,398 |
| Diabetes | 12,495 | \$ 5,942,870 |
| Osteoarthritis | 10,244 | \$ 16,757,042 |
| Mental Health—Depression | 6,872 | \$ 3,065,655 |
| Coronary Artery Disease | 5,563 | \$ 24,911,347 |
| Asthma | 4,535 | \$ 1,657,354 |
| Mental Health—Anxiety Disorder | 2,789 | \$ 463,338 |
| Obstructive Pulmonary Disease | 2,550 | \$ 2,151,242 |
| Mental Health—Bipolar Disorder | 1,335 | \$ 1,143,225 |
| Congestive Heart Failure | 1,069 | \$ 3,883,407 |
| Rheumatoid Arthritis | 890 | \$ 1,522,576 |
| HIV Infection | 157 | \$ 158,787 |

Medical costs represent the amount paid by the plan for facility and professional services provided under medical coverage (excluding prescription drugs). Data represents 2006 paid claims.

Benefits Distribution by Provider Type (Paid Claims)

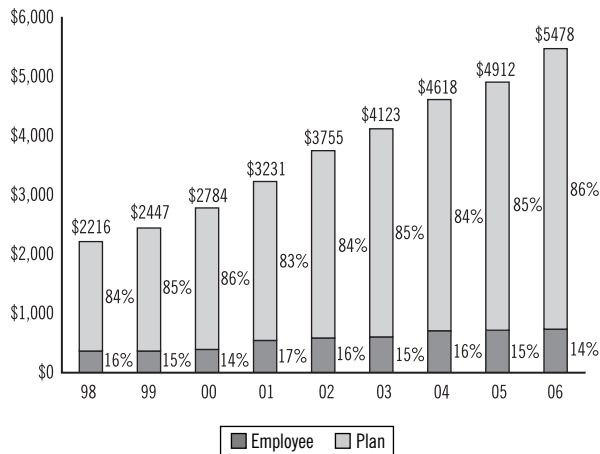
PPO, POS and HMO total disbursements: \$627,343,429 (amount reflects all health vendors submitting data for 2006)

Total self-insured paid claims for 2006 increased from \$525,088,735 in 2005. As a percent of the total, there was a slight decrease in payments to physicians and a slight increase in payments to pharmacies.



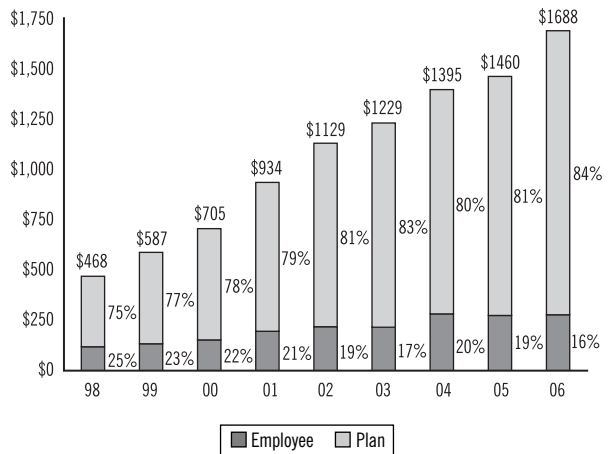
PPO Per Capita Payments

Employee portion represents deductibles and coinsurance/copays. Percentages indicate portion of medical expenses paid by the employee and the plan.



PPO Per Capita Drug Payments

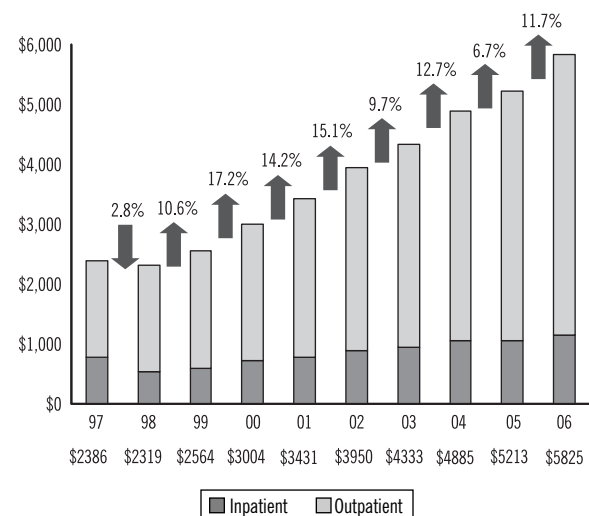
Employee portion represents deductibles and coinsurance/copays. Percentages indicate portion of pharmacy expenses paid by the employee and the plan.



PPO Total Payments Per Capita

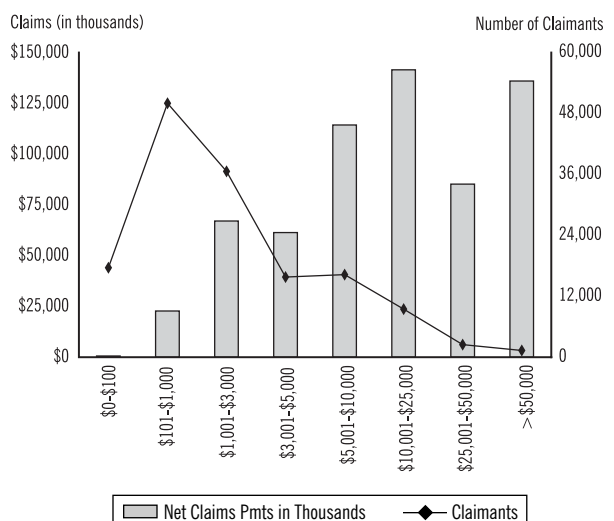
Includes all plan payments and patient payments for deductibles and copayments (incurred data).

For 2006, payments for outpatient services represented 80 percent of the total — up from 68 percent in 1997. Outpatient payments grew at a rate of 21 percent per year between 1997 and 2006. Payments for inpatient services grew at almost 6 percent per year.



Paid Claims Distribution by Individual

About 9 percent of the plan members received benefits in excess of \$10,000 and accounted for 58 percent of the benefit payments. The average benefit for this group was \$27,273.



Wellness Program

The State Employee Wellness Program was initiated in 1992. It is designed to improve awareness of the factors that can affect health and longevity, as well as to enable employees to take increased responsibility for their health by adopting healthier lifestyles. The program is funded, in part, through flexible benefits savings. The information on this page provides components and participation for the various programs offered.

Screenings and Health Risk Assessments

In 2006, 3,076 individuals attended a health screening and completed a health risk assessment (HRA). The average participant age was 47 with 42.5 percent of participants being male and 57.5 percent female.

Health Risks by Prevalence

| | |
|--------------------------------|-------|
| Body Weight | 52.9% |
| Blood Pressure | 40.6% |
| Stress | 30.5% |
| Safety Best Use | 26.3% |
| Medication/Drug for Relaxation | 23.3% |
| Life Satisfaction | 19.3% |
| Physical Activity | 17.1% |
| Illness Days | 14.5% |
| Perceived Health | 13.4% |
| Job Satisfaction | 11.8% |
| Existing Medical Conditions | 11.6% |
| Smoking | 11.3% |
| Cholesterol | 10.2% |
| Alcohol | 1.2% |

Coaching

Employees participating in the health screenings and HRA who were identified as having two or more high risks were invited to participate in the wellness coaching or high-risk intervention program — 31 percent of those eligible to participate enrolled. Each participant received intervention telephone calls and follow-up calls from a qualified health educator or RN over a six-month period. A total of 178 participants, or 52 percent, have improved or eliminated between one and three risk factors.

Toll-Free HealthLine

The HealthLine made 3,288 calls. Health educators answer this line and initiate calls to participants as well.

Seminar Series

During 2006, two new titles were added to the seminar program: Cholesterol and Diabetes Myths and Happiness 101, bringing the total number of available seminars to 16. A total of 1,668 employees participated in one or more of the seminars presented.

Babies First Prenatal Program

Designed to encourage early prenatal care, the program is open to female employees, spouses and dependents enrolled in health coverage administered by BlueCross BlueShield. The program provides a \$50 credit or refund to the mother's deductible and copies of two books dealing with newborns. Participation in the program totaled 60 in 2006.

Fitness Center Discount Program

Over 100 fitness centers across the state provide membership discounts to participants in the state group insurance program.

Winter Games Challenge

This 10-week program was designed to encourage participants to incorporate exercise into their daily routine. A total of 2,276 employees registered with 652, or 29 percent, completing the program. Participants who completed exercise logs reported 19,654 hours of exercise and, on average, saw a weight loss of 7.3 pounds. At the onset of the program, 49 percent of participants identified themselves as exercising no more than one day per week, 26 percent identified themselves as exercising two to three days per week and 24 percent identified themselves as exercising four or more days per week. At the conclusion of the program, 76 percent reported exercising between five and seven days per week.

Maintain Don't Gain Challenge

This challenge encouraged participants not to gain the average six to seven pounds from Thanksgiving to New Year's Day and maintain their pre-holiday weight. A total of 1,049 employees registered with 481, or 46%, completing the program. Results showed a total of 843 pound lost — an average of 1.8 pounds per participant.

Local Education Plan

In 1985, the Tennessee General Assembly authorized creation of an insurance plan for local education employees. Funds were appropriated to pay part of the premiums for participating employees beginning January 1, 1986. School systems within the state may join the local education plan or must provide alternative coverage that is equal or superior to the state-sponsored program.

At 2006 year end, 124 school systems and educational co-ops were participating in the local education plan. Plan enrollment was 50,929 — up from 49,635 in 2005. The portion of plan members selecting the POS option continued to increase, growing from 18,805 to 18,953. PPO enrollment decreased from 25,411 to 24,115 while HMO selection increased from 5,419 to 7,861.

Dental insurance is available as an option to participants in the local education plan. Participation in the dental plan increased from 6,071 to 6,377.

Life insurance and long-term care coverage are not available options to members in the self-insured local education plan.

In 2006, there was a 12 percent increase in the total allowed amount per member in the PPO to \$4,993. The increase was mostly attributable to increasing outpatient costs, as the total allowed amount per outpatient medical service increased 12 percent to \$69 and the total allowed amount per member for outpatient medical and pharmacy payments increased 12 percent to \$4,079.

Total allowed amounts per member in the POS increased 14 percent primarily due to increasing inpatient expenses, while the total allowed amounts per member in the HMO increased 13 percent over 2005.

Pharmacy costs continue to impact the growth of benefit payments in the local education plan. For the PPO, the plan's cost for prescription drugs for each member increased from \$1,023 in 2005 to \$1,224 in 2006 — a 20 percent increase. As costs continue to increase, the plan will have to continually review its benefits, with the goal of providing value to plan members while at the same time sharing benefit expenses appropriately.

Health Contracts

Preferred Provider Organization (PPO)

| | | |
|----------------------|--------|-------|
| BlueCross BlueShield | 24,115 | |
| Percent of Total | | 47.4% |

Health Maintenance Organization (HMO)

| | | |
|---------------------------------|-------|------|
| Nashville — Cigna Healthcare | 590 | |
| Percent of Total | | 1.2% |
| Memphis — Cigna Healthcare | 346 | |
| Percent of Total | | 0.7% |
| Knoxville — United Healthcare | 3,603 | |
| Percent of Total | | 7.1% |
| Chattanooga — United Healthcare | 615 | |
| Percent of Total | | 1.2% |
| Tri-Cities — United Healthcare | 2,707 | |
| Percent of Total | | 5.3% |

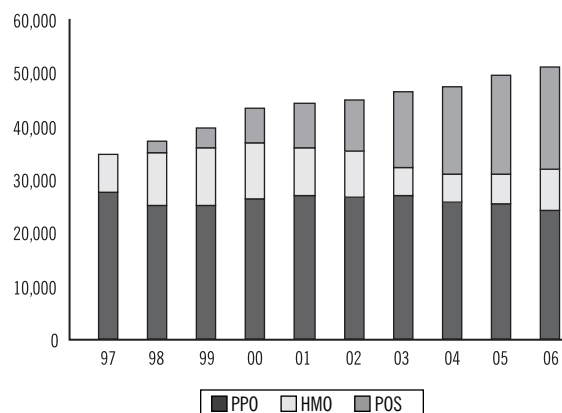
Point of Service (POS)

| | | |
|---------------------------|-------|-------|
| West — Cigna Healthcare | 3,896 | |
| Percent of Total | | 7.6% |
| Middle — Cigna Healthcare | 7,824 | |
| Percent of Total | | 15.4% |
| East — Cigna Healthcare | 7,233 | |
| Percent of Total | | 14.2% |

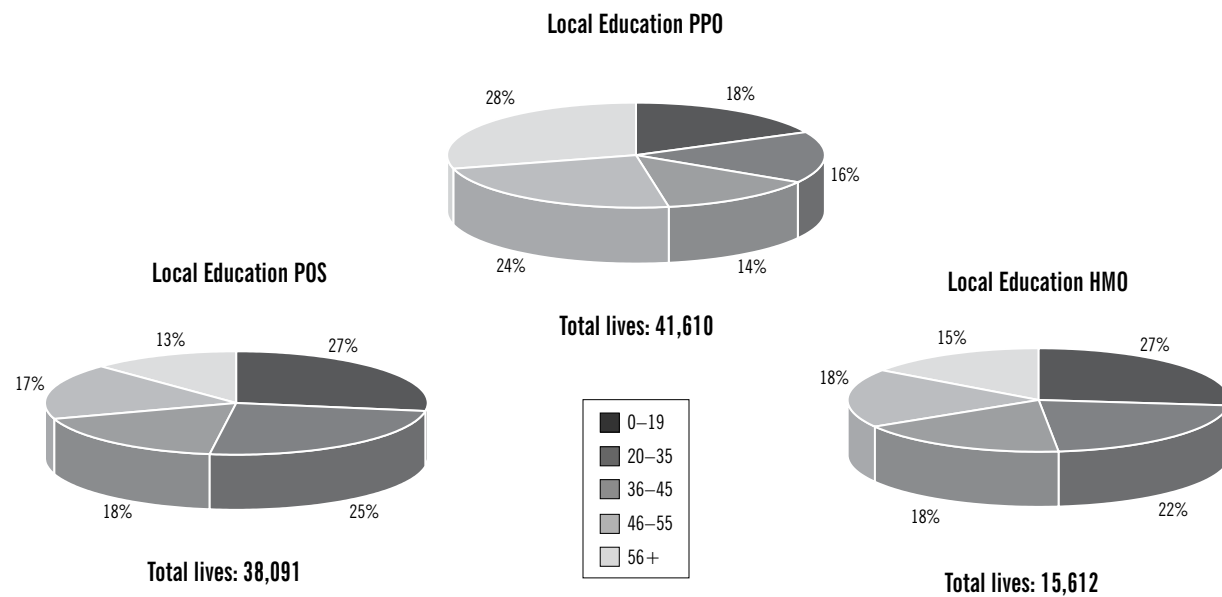
Optional Insurance Contracts

| | DEC. 31, 2006 | DEC. 31, 2005 |
|-------------------------------|---------------|---------------|
| Dental Insurance | | |
| Prepaid Plan | 1,597 | 1,611 |
| Preferred Provider Plan | 4,780 | 4,460 |
| Total Dental Insurance | 6,377 | 6,071 |

Total Contracts by Healthcare Option



Health Enrollment Demographics



Chronic Conditions—Patients and Medical Costs

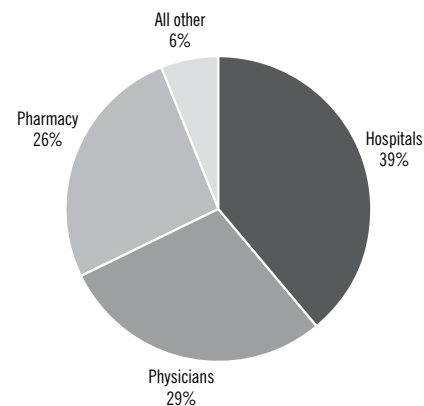
| | TOTAL PATIENTS | TOTAL COSTS |
|--------------------------------|----------------|---------------|
| Hypertension | 14,972 | \$ 2,735,332 |
| Diabetes | 6,223 | \$ 2,801,091 |
| Osteoarthritis | 5,762 | \$ 9,481,222 |
| Mental Health—Depression | 3,275 | \$ 1,168,193 |
| Coronary Artery Disease | 2,682 | \$ 11,645,962 |
| Asthma | 2,622 | \$ 709,818 |
| Mental Health—Anxiety Disorder | 1,605 | \$ 241,177 |
| Obstructive Pulmonary Disease | 1,182 | \$ 613,835 |
| Rheumatoid Arthritis | 551 | \$ 722,935 |
| Mental Health—Bipolar Disorder | 534 | \$ 413,078 |
| Congestive Heart Failure | 420 | \$ 864,901 |
| HIV Infection | 36 | \$ 44,059 |

Medical costs represent the amount paid by the plan for facility and professional services provided under medical coverage (excluding prescription drugs). Data represents 2006 paid claims.

Benefits Distribution by Provider Type (Paid Claims)

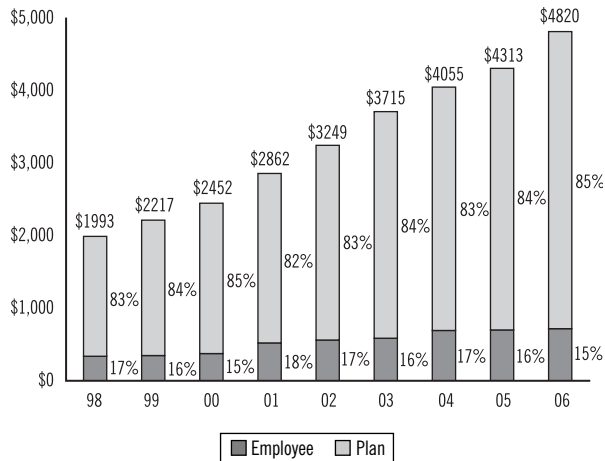
PPO, POS and HMO total disbursements: \$346,942,498 (amount reflects all health vendors submitting data for 2006)

Total self-insured paid claims for 2006 increased from \$293,685,864 in 2005. As a percent of the total, payments to hospitals and physicians were basically flat when compared to 2005, while there was a slight increase in payments to pharmacies.



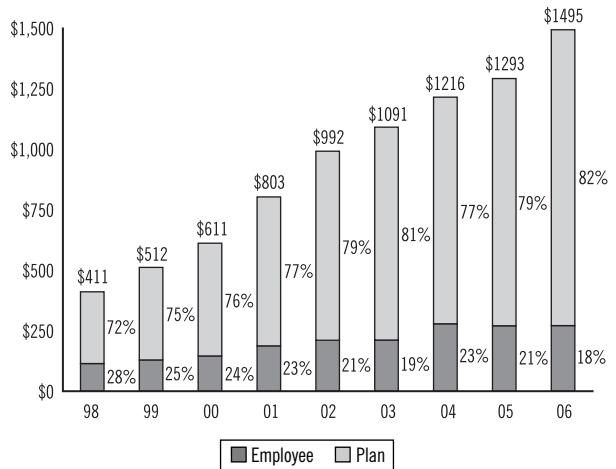
PPO Per Capita Payments

Employee portion represents deductibles and coinsurance/copays. Percentages indicate portion of medical expenses paid by the employee and the plan.



PPO Per Capita Drug Payments

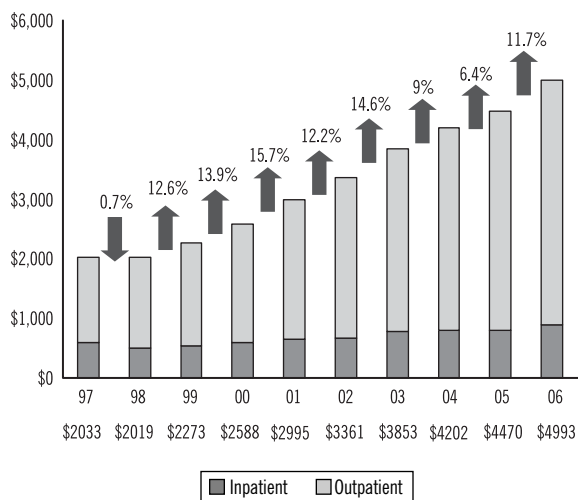
Employee portion represents deductibles and coinsurance/copays. Percentages indicate portion of pharmacy expense paid by the employee and the plan.



PPO Total Payments Per Capita

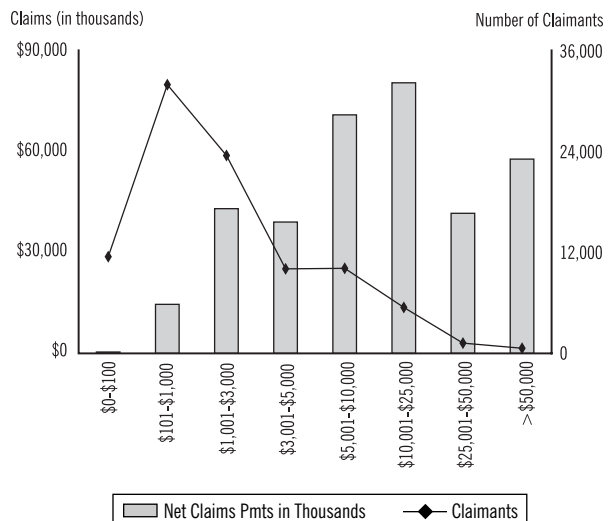
Includes all plan payments and patient payments for deductibles and copayments (incurred data).

For 2006, payments for outpatient services represented 82 percent of the total — up from 70 percent in 1997. Outpatient payments grew at a rate of almost 21 percent per year between 1997 and 2006. Payments for inpatient services grew at 5 percent per year.



Paid Claims Distribution by Individual

About 8 percent of the plan members received benefits in excess of \$10,000 and accounted for about 52 percent of the benefit payments. The average benefit for this group was \$24,608.



Participants

| | | | |
|-----------------------------------|--|----------------------------------|---------------------------------------|
| Alamo City Schools | Franklin County Schools | Lenoir City Schools | Putnam County Schools |
| Alcoa City Schools | Franklin Special School District | Lewis County Schools | Rhea County Schools |
| Anderson County Schools | Gibson County Schools | Lexington City Schools | Richard City Special Schools |
| Athens City Schools | Giles County Schools | Lincoln County Schools | Roane County Schools |
| Bedford County Schools | Grainger County Schools | Little TN Valley Education Co-op | Robertson County Schools |
| Bells City Schools | Greene County Schools | Loudon County Schools | Rogersville City Schools |
| Benton County Schools | Greenville City Schools | Macon County Schools | Scott County Schools |
| Bledsoe County Schools | Grundy County Schools | Manchester City Schools | Sequatchie County Schools |
| Bradford Special School District | Hamblen County Schools | Marion County Schools | Sevier County Schools |
| Bradley County Board of Education | Hancock County Schools | Marshall County Schools | Smith County Schools |
| Bristol City Schools | Hardeman County Schools | Maury County Schools | South Carroll County Special District |
| Campbell County Schools | Hardin County Schools | McKenzie Special School District | Stewart County Schools |
| Cannon County Schools | Hawkins County Schools | McMinn County Schools | Sullivan County Board of Education |
| Carroll County Schools | Haywood County Schools | McNairy County School System | Sumner County Board of Education |
| Carter County Schools | Henderson County Schools | Meigs County Board of Education | Sweetwater City Schools |
| Cheatham County Schools | Henry County Board of Education | Milan Special School District | Tipton County Schools |
| Chester County Schools | Hickman County Schools | Monroe County Board of Education | Trenton Special School District |
| Clay County Schools | Hollow Rock – Bruceton Special School District | Moore County Schools | Tri-County Vocational Schools |
| Cleveland City Schools | Houston County Schools | Morgan County Schools | Trousdale County Schools |
| Clinton City Schools | Humboldt City Schools | Murfreesboro City Schools | Tulahoma City Schools |
| Cocke County Schools | Humphreys County Schools | Newport City Schools | Unicoi County Schools |
| Coffee County Schools | Huntingdon Special Schools | Oak Ridge City Schools | Union City Schools |
| Crockett County Schools | Jackson County Schools | Obion County Schools | Union County Schools |
| Cumberland County Schools | Jackson-Madison County Board of Education | Oneida Special School District | Van Buren County Schools |
| Dayton City Schools | Jefferson County Schools | Overton County Schools | Warren County Schools |
| Decatur County Schools | Kingsport City Schools | Paris Special School District | Washington County Schools |
| Dekalb County Schools | Knox County Schools | Perry County Schools | Wayne County Schools |
| Dyer County Schools | Lake County Schools | Pickett County Schools | Weakley County Schools |
| Dyersburg City Schools | Lauderdale County Schools | Polk County Board of Education | West Carroll Special School District |
| Elizabethton City Schools | Lawrence County Schools | | White County Schools |
| Etowah City Schools | Lebanon – Tenth District Schools | | |
| Fayette County Schools | | | |
| Fayetteville City Schools | | | |
| Fentress County Schools | | | |

Local Government Plan

In 1989, the Tennessee General Assembly authorized creation of an insurance plan for local government agency and quasi-governmental agency employees. At 2006 year end, 374 counties, cities and quasi-governmental agencies were participating in the local government plan. This number reflects 34 new agencies joining the plan and 14 terminating participation during the year.

Plan enrollment was 12,902 at year end, a decrease from 14,625 in December 2005. Of the total enrollment, 3,916 participated in the PPO, while 2,774 were covered by HMOs. Enrollment in POSs totaled 5,519. The high deductible PPO limited option established at the beginning of 2004 had a total enrollment of 693 at year end.

Dental insurance became available as an option to participants in the local government plan in January 1993. Participation in the dental coverage at year end was 2,159.

Life insurance and long-term care coverage are not available options to members in the self-insured local government plan.

There was a 16 percent increase — to \$6,180 — in the allowed amount per PPO member during 2006. This increase was mostly attributable to strong increases in inpatient activity, both in terms of cost and use. Total payments between plan members and the plan for inpatient activity for all PPO members increased 9 percent to \$1,512, while the number of inpatient days per 1,000 members increased 10 percent to 488.

Total allowed amounts per member in the POS were \$5,005 — up 21 percent over 2005. This was driven mostly by large increases in inpatient cost and use as in the PPO, as well as significant increases in payments per service for outpatient activity.

Pharmacy costs continue to impact the growth of benefit payments in the local government plan. For the PPO, the plan's cost for prescription drugs for each member increased from \$1,047 in 2005 to \$1,329 in 2006 — a 27 percent increase. As costs continue to increase, the plan will have to continually review its benefits, with the goal of providing value to plan members while at the same time sharing benefit expenses appropriately.

Health Contracts

Preferred Provider Organization (PPO)

| | | |
|----------------------|-------|-------|
| BlueCross BlueShield | 3,916 | |
| Percent of Total | | 30.4% |

Health Maintenance Organization (HMO)

| | | |
|---------------------------------|-----|------|
| Nashville — Cigna Healthcare | 280 | |
| Percent of Total | | 2.2% |
| Memphis — Cigna Healthcare | 568 | |
| Percent of Total | | 4.4% |
| Knoxville — United Healthcare | 838 | |
| Percent of Total | | 6.5% |
| Chattanooga — United Healthcare | 727 | |
| Percent of Total | | 5.6% |
| Tri-Cities — United Healthcare | 361 | |
| Percent of Total | | 2.8% |

Point of Service (POS)

| | | |
|---------------------------|-------|-------|
| West — Cigna Healthcare | 1,490 | |
| Percent of Total | | 11.5% |
| Middle — Cigna Healthcare | 2,583 | |
| Percent of Total | | 20.0% |
| East — Cigna Healthcare | 1,446 | |
| Percent of Total | | 11.2% |

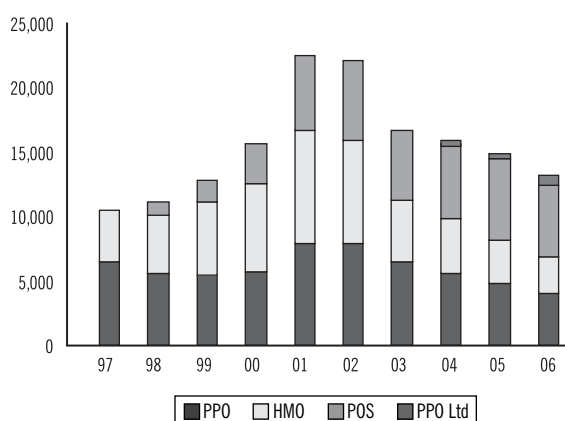
Preferred Provider Organization Limited (PPO Ltd)

| | | |
|----------------------|-----|------|
| BlueCross BlueShield | 693 | |
| Percent of Total | | 5.4% |

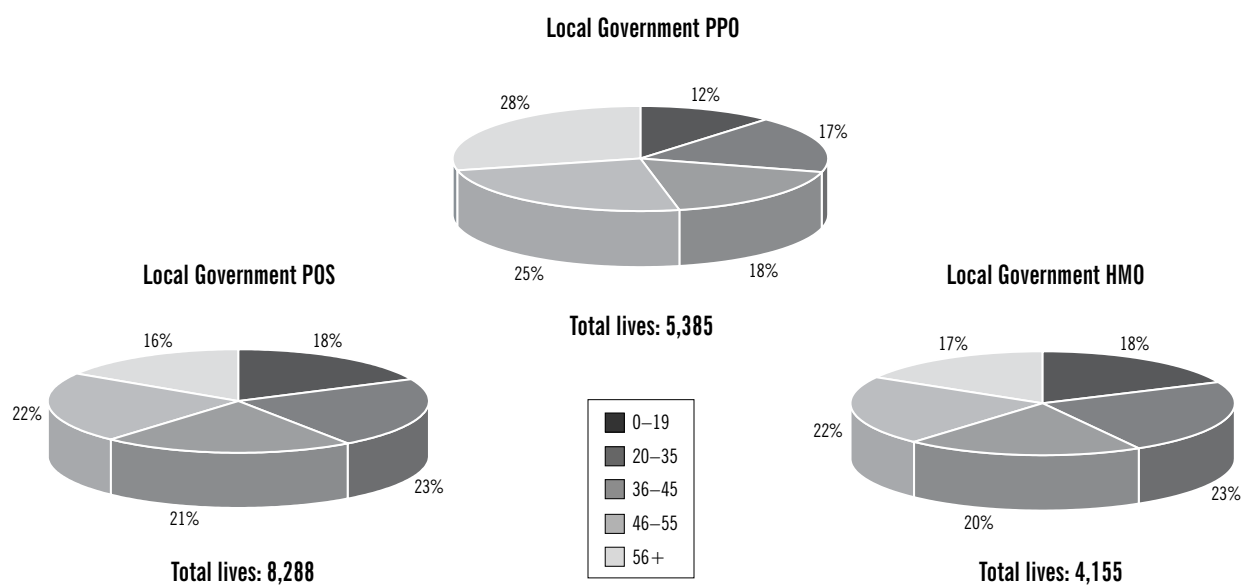
Optional Insurance Contracts

| | DEC. 31, 2006 | DEC. 31, 2005 |
|-------------------------------|---------------|---------------|
| Dental Insurance | | |
| Prepaid Plan | 928 | 979 |
| Preferred Provider Plan | 1,231 | 1,132 |
| Total Dental Insurance | 2,159 | 2,111 |

Total Contracts by Healthcare Option



Health Enrollment Demographics



Chronic Conditions—Patients and Medical Costs

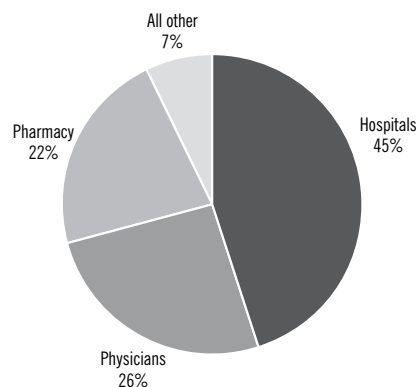
| | TOTAL PATIENTS | TOTAL COSTS |
|--------------------------------|----------------|--------------|
| Hypertension | 4,007 | \$ 798,385 |
| Diabetes | 1,932 | \$ 782,515 |
| Osteoarthritis | 1,540 | \$ 2,939,133 |
| Coronary Artery Disease | 939 | \$ 5,493,049 |
| Mental Health—Depression | 809 | \$ 284,368 |
| Asthma | 580 | \$ 223,127 |
| Obstructive Pulmonary Disease | 449 | \$ 341,026 |
| Mental Health—Anxiety Disorder | 423 | \$ 41,184 |
| Congestive Heart Failure | 168 | \$ 375,823 |
| Mental Health—Bipolar Disorder | 140 | \$ 107,697 |
| Rheumatoid Arthritis | 125 | \$ 225,955 |
| HIV Infection | 25 | \$ 24,602 |

Medical costs represent the amount paid by the plan for facility and professional services provided under medical coverage (excluding prescription drugs). Data represents 2006 paid claims.

Benefits Distribution by Provider Type (Paid Claims)

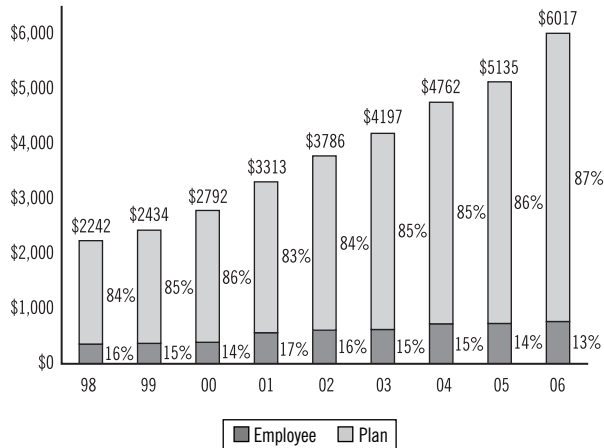
PPO, POS and HMO total disbursements: \$88,948,307 (amount reflects all health vendors submitting data for 2006)

Total self-insured paid claims for 2006 increased from \$87,328,610 in 2005. As a percent of the total, payments to hospitals increased when compared to 2005, while there was a decrease in payments to physicians.



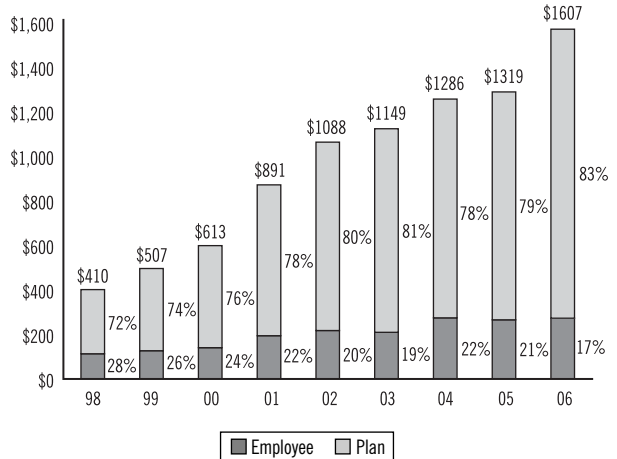
PPO Per Capita Payments

Employee portion represents deductibles and coinsurance/copays. Percentages indicate portion of medical expenses paid by the employee and the plan.



PPO Per Capita Drug Payments

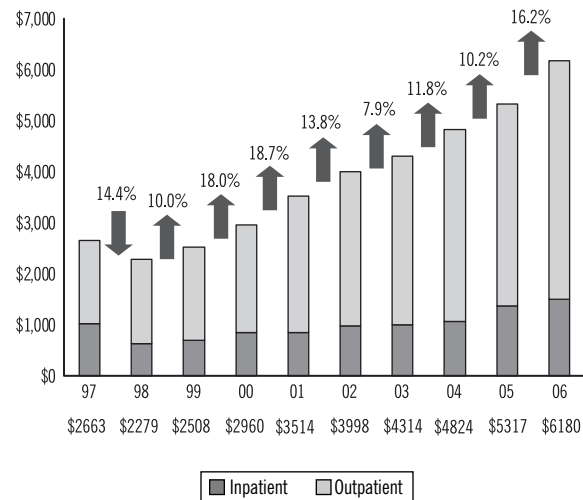
Employee portion represents deductibles and coinsurance/copays. Percentages indicate portion of pharmacy expense paid by the employee and the plan.



PPO Total Payments Per Capita

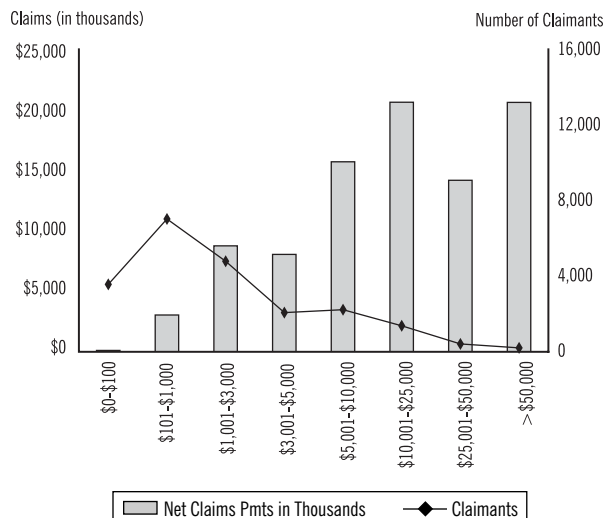
Includes all plan payments and patient payments for deductibles and copayments (incurred data).

For 2006, payments for outpatient services represented almost 76 percent of the total — up from 62 percent in 1997. Outpatient payments grew at a rate of 20 percent per year between 1997 and 2006. Payments for inpatient services grew 5 percent per year.



Paid Claims Distribution by Individual

About 9 percent of the plan members received benefits in excess of \$10,000 and accounted for about 61 percent of benefit payments. The average benefit for this group was \$27,754.



Participants

| | | | |
|---|--|---|---|
| Access Services of Middle TN | Center for Independent Living of Middle TN | East TN Foundation | Henderson County Highway |
| Adult Community Training | Center for Living and Learning | Eastside Utility District | Henry County Highway |
| Agape, Inc. | | Engstrom Services, Inc. | Hickman County |
| Aging Services of the Upper Cumberland | Centerville, Town of | Erin, City of | Highland Rim Economic Corporation |
| Aid Distressed Families – Anderson County | Chattanooga Boys Choir | Estill Springs, Town of | Hixson Utility District |
| Alamo, City of | Chattanooga Endeavors, Inc. | Etheridge, City of | Homeplace, Inc. |
| Alcohol and Drug Council of Middle TN | Children's Advocacy Center | Fairview Utility District | Homesafe of Sumner, Wilson and Robertson County |
| Alpha-Talbot Utility District | Claiborne County Highway | Fayette County 911 | Hope of East TN |
| Anderson County CAC | Clarksville Housing Authority | Fayette County | Humboldt Housing Authority |
| Anderson County Health Council | Clarksville/Montgomery County CAA | Fayette County Public Works | Humboldt, City of |
| Appalachian Education Community Corp. | Clearfork Utility District | Fayetteville Housing Authority | Humphreys County |
| ARC of Hamilton County | Clifton, City of | First Utility District of Tipton County | Humphreys County 911 |
| ARC of Washington County | Clinchfield Senior Center | First Utility of Hawkins County | Huntingdon, Town of |
| ARC of Williamson County | Cocke County | Forest Hill, City of | Impact Center, Inc. |
| Ashley's Place – Sumner Child Advocacy Center | Cocke County 911 | Four Lake Regional Industrial Development Authority | Jacksboro, Town of |
| Atoka, Town of | Cocke County Highway | Franklin Consolidated Housing Authority | Jackson Area Council on Alcohol and Drug Dependence |
| Atwood, Town of | Coffee County | Franklin County | Jackson Center for Independent Living |
| Avalon Center | Collegedale, City of | Franklin County Adult Activity Center | James Developmental Center |
| Bedford County | Community Anti-Drug Coalition Across TN | Franklin County Highway | Jason Foundation |
| Belle Meade, City of | Community Development Center | Franklin County Industrial Development Board | Jasper, Town of |
| Bells, City of | Community Network Services | Friendship, City of | Jefferson City Housing |
| Benton County Highway | Comprehensive Care Center | Gallatin Housing Authority | Jefferson County |
| Better Decisions | Coopertown, Town of | Gibson County Municipal Water | Jefferson County 911 |
| Big Creek Utility District | Cornerstone | Giles County | Johnson County |
| Big Sandy, City of | County Wide Utility District | Giles County 911 | Jubilee Community Arts |
| Bledsoe County | Crab Orchard Utility District | Gladeville Utility District | Kids Place – A Child Advocacy Center |
| Bloomington Utility | Crockett County | Gleason, City of | Kimball, Town of |
| Blount County CAA | Crockett County Highway | Good Neighbor Mission and Crisis Center | Kings Daughters Day Home |
| Bon Aqua Lyles Utility | Crockett Public Utility District | Goodwill Industries Knoxville, Inc. | Kingsport Housing and Redevelopment Authority |
| Bondcroft Utility | Cross Plains, City of | Gordonville, Town of | Kingston, City of |
| Bradley County | Cumberland Community Options, Inc. | Greenbrier, City of | Kingston Springs, Town of |
| Bradley/Cleveland CSA | Cumberland County | Grundy County | Knoxville-Knox County CAC |
| Bradley/Cleveland Services | Cumberland Heights | Grundy County Highway | Lafayette, City of |
| Bridge Refugee Services | Cumberland Utility District | Grundy Emergency Medical Services | Lakeland, City of |
| Bridges of Williamson County | Cunningham Utility District | Grundy Housing Authority | Lakesite, City of |
| Bruceton, Town of | Dayton, City of | Hamilton County 911 | Lauderdale County |
| Burns, City of | Decatur County | Hardeman – Fayette Utility District | Lawrence County |
| Camden, City of | Decaturville, Town of | Hardin County Government | Lawrence County 911 |
| Camden, City of | Decherd, City of | Hardin County Skills, Inc. | Lawrence County Chamber of Commerce |
| Campbell County 911 | Dekalb County | Harriman, City of | Lawrenceburg, City of |
| Care of Savannah, Inc. | DeWhite Utility | Hartsville/Trousdale County | Lawrenceburg Housing Authority |
| Carroll County 911 | Dickson Electric Department | Hawkins County | Lewis County Highway |
| Carthage, Town of | Disability Resource Center | Haywood County | Lewisburg Housing Authority |
| Caryville – Jacksboro Utility | Dover, Town of | Haywood County Highway | Lexington, City of |
| Caryville, Town of | Downtown Ministry Center, Inc. | Henderson, City of | Lexington Electric System |
| CASA – Juvenile Services | Dresden, City of | Henderson County | Lincoln County |
| CASA of the TN Heartland | Dunlap, City of | | Linden, City of |
| CASA, Inc. | East Ridge, City of | | |
| Castalian Springs – Bethpage Utility District | East TN CSA | | |
| CEASE, Inc. | East TN Development District | | |

| | | | |
|--|--|--|---|
| Lobelville, City of | Oak Ridge Housing Authority | Soddy-Daisy Falling Water Utility | TN Organization of School Superintendents |
| Loretto, City of | Old Hickory Utility | South Carthage, Town of | TN Primary Care Association |
| Lynnville, City of | Old Knoxville Highway Water District | South Central CSA | TN School Board Association |
| Madison Suburban Utility | Orange Grove Center | South Central TN Development District | TN Secondary School Athletic Association |
| Manchester Housing Authority | Overton County | South Central TN Workforce Board | TN State Employees Association |
| Marion County | Overton County Highway | South Pittsburg, City of | TN State Museum Foundation |
| Marion County Highway | Overton County Nursing Home | Southeast Mental Health Center | TN State Veterans Home – Humboldt |
| Marion County 911 | Parsons, City of | Southeast Regional CHA | TN State Veterans Home – Knoxville |
| Marion Natural Gas | Pathfinders, Inc. | Southwest CHA | TN State Veterans Home – Murfreesboro |
| Mason, Town of | Pegram, Town of | Sparta Electric and Water System | Tracey City Public Utility |
| McKenzie, City of | Perry County Highway | Spectrum Support Services | Tri-Cities/Sullivan Utility District |
| McNairy County | Perry County Officials | Spring City, Town of | Troy, Town of |
| McNairy County Highway | Petersburg, Town of | St. Joseph, City of | Tullahoma Housing Authority |
| Memphis and Shelby County CSA | Pleasant View, Town of | Statewide Independent Living Council of TN | Tullahoma Utilities |
| Memphis Center for Independent Living | Portland, City of | Stewart County | Twenty-first Drug Task Force |
| Mental Health Association of Middle TN | Powells Crossroad, Town of | Stewart County Highway | Unicoi, Town of |
| Mid-Cumberland CAA | Professional Educators of TN | Street Works | Union City Electric System |
| Mid-Cumberland CHA | Puryear, City of | Sullivan County 911 | Union County Highway |
| Mid-Cumberland HRA | Putnam County Rural Health Clinic | Surgoinsville Utility District | United Cerebral Palsy Center |
| Mid-East CAA | Rape and Sexual Abuse Center | TARP, Inc. | Upper Cumberland CSA |
| Milan Public Utilities | Reelfoot Lake Regional Utility and Planning District | Team Evaluation Center | Upper Cumberland Development District |
| Ministerial Association | Rhea County | Temporary Residence for Adolescents and Crisis | Upper East TN Human Development Agency |
| Temporary Shelter | Rhea Medical Center | TennCare Consumer Advocacy Program | Urban Housing Solutions |
| Minor Hill Water Utility District | Riceville Utility District | Tennessee Tomorrow | Vital Center |
| Monteagle, Town of | Ripley, City of | Tennessee Voices for Children | Volunteer Memphis |
| Mosheim, Town of | Ripley Gas/Water | Tipton County | Walden, Town of |
| Mt. Carmel – Hawkins SCC | Roane Central Utility | Tipton County 911 District | Warren County |
| Murfreesboro Electric Department | Roane County | Tiptonville, Town of | Wartburg, City of |
| NAMI TN | Roane County 911 | TN Alcohol and Drug Association | Wartrace, Town of |
| Nashville Cares | Rochelle Center | TN Association for Child Care | Waverly, City of |
| Nashville Cares – Special Funding | Rose Center Council for the Arts | TN Arts Center of Cannon County | WDVX Cumberland Communications |
| National Association of Social Workers | Rossville, Town of | TN Association of County Executives | Weakley County |
| National Healthcare for the Homeless Council | Rutherford County Adult Action Center | TN Association of Craft Artists | Weakley County 911 |
| New Directions | Safe Haven Center | TN Association of Utility Districts | Webb Creek Utility |
| New Horizons Corporation | Savannah, City of | TN Business Enterprises | West Cumberland Utility |
| New Johnsonville, City of | Scotts Hill, Town of | TN Center for Nursing, Inc. | West Overton Utility |
| New Market Utility District | Second South Cheatham Utility District | TN Chapter of Children's Advocacy Center | West TN Legal Services, Inc. |
| North Utility of Decatur/Benton County | Senior Citizens, Inc. | TN County Commissioners Association | West TN Regional Art Center |
| Northeast CSA | Sequatchie County | TN County Highway Officials | West Warren – Viola Utility |
| Northeast Henry County Utility | Sequatchie Valley Planning | TN County Services Association | White Bluff, City of |
| Northwest CHA | Serenity Recovery Center | TN Healthcare Campaign | Whitwell, City of |
| Northwest Dyersburg Utility | Sertoma Center | TN Historical Society | Williamson County Child Advocacy Center |
| Northwest Safeline | Sharon, City of | TN Mental Health Consumers Association | Winchester, City of |
| Northwest TN Economic Development Council | Shelby County 911 | | Woodbury Housing Authority |
| Northwest TN Head Start | Shelby Residential and Vocational Services, Inc. | | Workforce Solutions |
| Oak Ridge, City of | Shelter, Inc. | | |
| | Smith County | | |
| | Smith County Highway | | |
| | Smithville, City of | | |
| | Smithville Electric System | | |

Employee Assistance Program

The EAP provides counseling and referral services for personal and workplace problems. Eligible employees and their dependents may receive up to six counseling sessions per problem episode at no direct cost. The program is available to all state and higher education employees/dependents who are eligible to participate in the state group insurance program and all local education and local government employees who participate in a state-sponsored health plan. If more intensive treatment is needed, individuals may receive care through their insurance plan's mental health or substance abuse coverage.

Magellan Health Services reported 14,504 members accessing EAP services for the year. EAP counseling referrals totaled 6,216, indicating a 4.4 percent utilization rate for individual counseling sessions.

Training programs include employee orientations and supervisory training classes on the EAP services. Personal and professional growth seminars are held in nine locations across the state quarterly and upon request by agencies, departments and schools. Participation in consultation and training services continues to be in high demand. A total of 744 hours were spent in training activities reaching 13,152 employees. Supervisory training ses-

sions are offered to teach supervisors how to use the EAP as one of their managerial tools in promoting good job performance. A total of 54 sessions were provided with attendance totaling 870. Critical stress debriefings occurred on 48 occasions involving 234 sessions with 801 employees. This was a significant increase from the previous year of 27 occasions involving 121 sessions with 556 employees. There were 254 professional and personal growth seminars offered and attended by 5,984 employees. On-line services at the Magellan website were frequented by 8,685 employees

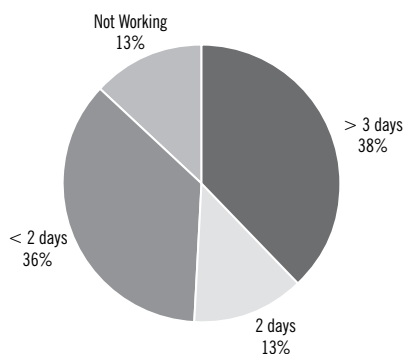
Employee Utilization

| | |
|---------------------------------|------|
| Counseling Services Utilization | 4.0% |
| Training Utilization | 8.7% |

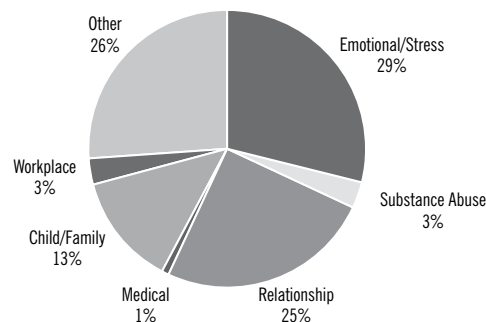
EAP Referral Utilization by Plan

| | |
|-----------------------|-----|
| State Plan | 78% |
| Local Education Plan | 16% |
| Local Government Plan | 6% |

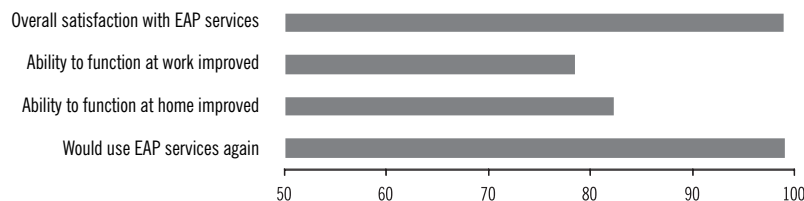
Estimated Loss of Work Without EAP Services



Problem Types of New Cases



EAP Client Office Session Questionnaire Responses



Mental Health and Substance Abuse

The management of mental health and substance abuse benefits through Magellan Health Services for the integrated employee assistance and behavioral health program has continued to result in patients receiving care in more clinically appropriate and less costly settings. As noted in the data, inpatient utilization, as reflected in admissions and days of care per 1,000 plan members, decreased from 2005 to 2006. Partial hospital rates and intensive outpatient rates increased. However, through a combination of improved benefit design and improved clinical management, quality and access to appropriate levels of care continues to improve as well as maintaining appropriate cost.

Total Utilization and Cost Summary — PPO and POS Combined Plans

| | | AMOUNT PAID 2006 |
|--|--------|--------------------|
| Outpatient Sessions | 63,924 | \$2,808,930 |
| Intensive Outpatient/ Partial Hospitalization | 3,944 | 651,997 |
| Inpatient Days | 6,524 | <u>3,672,073</u> |
| | | <u>\$7,133,000</u> |

Inpatient Utilization — PPO and POS Combined Plans

| | 2006 | 2005 |
|--------------------------|------|------|
| Number of Cases Reviewed | 688 | 726 |
| Admissions per 1000* | 3.6 | 4.2 |
| Days per 1,000* | 3.0 | 33.1 |

*per 1,000 covered individuals

Outpatient Utilization — PPO and POS Combined Plans

| | PATIENTS REVIEWED | | SESSIONS PER 1,000* | |
|--|-------------------|-------|---------------------|------|
| | 2006 | 2005 | 2006 | 2005 |
| Outpatient | 8,517 | 8,314 | 294 | 312 |
| Intensive Outpatient/ Partial Hospitalization | 310 | 231 | 18.2 | 18.1 |

*per 1,000 covered individuals

Medicare Supplement Program

Since January 1989, the state has maintained a benefits program for medicare-eligible, retired teachers and state employees. The program involves two elements: the sponsorship of medicare supplement coverage and the provision of financial support for participating retirees.

The Medicare Modernization Act made significant changes to medicare and to the rules that govern medicare supplement coverage. It also authorized the new Medicare Part D prescription drug coverage. Based on the restrictions on the benefits that can be provided by medicare supplement policies, all participants were combined into a single medicare supplement plan — The Tennessee Plan — with previous pharmacy benefits subsequently discontinued. To comply with standard plan requirements established by the National Association of Insurance Commissions (NAIC), The Tennessee Plan matches the NAIC level D benefits.

Persons who had previously been enrolled in Plan Two or Plan Three had their premiums reduced to reflect the value of no longer having a pharmacy component as part of the benefit package. Members who had previously participated in Plan Two saw their premium reduced from a maximum of \$162 in 2005 to a maximum of \$105 in 2006, while those who had been in Plan Three saw their premium reduced from a maximum of \$307 in 2005 to a maximum of \$105 in 2006. Finally, those who stayed enrolled in Plan One had an overall increase in premium from \$82 to \$95, as the insurance committees sought to level premiums as much as possible, while giving those who were continuously enrolled in Plan One a slight reduction in premium in exchange for being commingled with all other plan members.

The state's financial support is based on a retiree's length of service. At the beginning of 2006, retired teachers and state employees received \$50 a month toward their premium if they had 30 or more years of service. For 20 to 29 years of service, they received \$30 a month; for 15 to 19 years of service, they received \$20 per month.

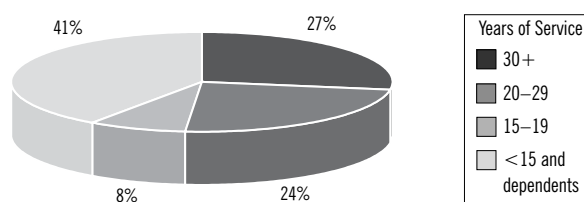
Based on legislation passed in 2006, the contribution rates increased effective August 2006 to \$50 per month for 30 or more years of service; \$37.50 for 15 to 19 years of service

and \$25 per month for 15 to 19 years of service. This support is provided to medicare supplement participants and to retired teachers in school districts which sponsor employee medical plans and permit medicare eligible retirees to continue coverage during retirement. Enrollment in this coverage decreased from 23,578 in 2005 to 21,923 in 2006.

The contract with BlueCross BlueShield for this coverage has contained a requirement that excess premiums be refunded to the state program on behalf of participating retirees. Half the excess premiums are returned at the end of the year; the balance at the end of the contract. Through the end of 2001, over \$27 million had been returned to the state under this contract requirement that was added at the beginning of 1992. These funds have resulted in reduced premiums for participating retirees through direct payment of part of the monthly retiree contribution.

Beginning in 2001, the program changed to a self-insured plan with payment of an administrative fee to BlueCross to pay for claims processing and customer service. Funds previously returned to the state or resulting from the 2001 year operation have been obligated to establish reserves for incurred but unreported claims and for claims expense fluctuations. By making these changes, administrative expenses were lowered, premium taxes were avoided and premium levels were more closely matched to anticipated benefit payments.

The Tennessee Plan Enrollment



Total lives: 21,923

FINANCIAL STATEMENTS

The following unaudited financial statements for the state plan, local education plan, local government plan and medicare supplement program disclose the financial position and the results of operations for the year ended June 30, 2006. The Department of Finance and Administration, Division of Insurance Administration prepared these statements which summarize transactions for all coverages available through each plan. The complete financial

statements, accompanying notes and supplemental schedules are included in the Comprehensive Annual Financial Report (CAFR) for the State of Tennessee. The CAFR was prepared by the Department of Finance and Administration, Division of Accounts and was audited by the Comptroller of the Treasury, Division of State Audit.

State Plan — Comparative Statement of Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------|-----------------------|-----------------------|
| Assets | | |
| Cash | \$ 216,105,609 | \$ 174,594,498 |
| Insurance accounts receivable | 1,538 | 1,717 |
| Accounts receivable | 2,948,747 | 1,285,124 |
| Total assets | \$ 219,055,894 | \$ 175,881,339 |
| Liabilities | | |
| Accrued liabilities | \$ 46,775,000 | \$ 40,172,000 |
| Accounts payable | 672,785 | 401,526 |
| Deferred revenue | 36,253,886 | 34,158,496 |
| Total liabilities | \$ 83,701,671 | \$ 74,732,022 |
| Net assets | | |
| Unrestricted | \$ 135,354,223 | \$ 101,149,317 |
| Total net assets | \$ 135,354,223 | \$ 101,149,317 |

State Plan — Comparative Statement of Revenues, Expenses and Changes in Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------------|-----------------------|-----------------------|
| Operating revenues | | |
| Premiums | \$ 644,383,797 | \$ 595,693,720 |
| Other | 182 | 21 |
| Total operating revenues | \$ 644,383,979 | \$ 595,693,741 |
| Operating expenses | | |
| Benefits/claims | \$ 581,670,171 | \$ 499,711,186 |
| Less: insurance recoveries | (8,407,291) | (9,647,291) |
| Administrative services | 2,896,454 | 2,684,772 |
| Contract services | 33,436,463 | 39,235,826 |
| Insurance premiums | 9,093,205 | 7,804,831 |
| Total operating expenses | \$ 618,689,002 | \$ 539,789,324 |
| Operating income | \$ 25,694,977 | \$ 55,904,417 |
| Non-operating revenues | | |
| Interest income | \$ 7,939,927 | \$ 2,977,665 |
| Total non-operating revenues | \$ 7,939,927 | \$ 2,977,665 |
| Income before transfers | \$ 33,634,904 | \$ 58,882,082 |
| Transfers from general fund | 570,002 | 487,306 |
| Change in net assets | \$ 34,204,906 | \$ 59,369,388 |
| Net assets, July 1 | 101,149,317 | 41,779,929 |
| Net assets, June 30 | \$ 135,354,223 | \$ 101,149,317 |

State Plan — Comparative Statement of Cash Flows

| | 30-JUN-06 | 30-JUN-05 |
|---|-----------------------|-----------------------|
| Cash flows from operating activities | | |
| Receipts from interfund services provided | \$ 412,772,088 | \$ 381,380,074 |
| Receipts from customers and users | 249,326,831 | 235,596,663 |
| Payments to suppliers | (626,201,283) | (562,015,309) |
| Payments for interfund services used | (2,896,454) | (2,684,772) |
| Net cash from (used for) operating activities | \$ 33,001,182 | \$ 52,276,656 |
| Cash flows from noncapital financing activities | | |
| Transfers in | \$ 570,002 | \$ 487,306 |
| Net cash from noncapital financing activities | \$ 570,002 | \$ 487,306 |
| Cash flows from investing activities | | |
| Interest received | \$ 7,939,927 | \$ 2,977,665 |
| Net cash from investing activities | \$ 7,939,927 | \$ 2,977,665 |
| Net increase (decrease) in cash and cash equivalents | \$ 41,511,111 | \$ 55,741,627 |
| Cash and cash equivalents, July 1 | 174,594,498 | 118,852,871 |
| Cash and cash equivalents, June 30 | \$ 216,105,609 | \$ 174,594,498 |
| Reconciliation of operating income to net cash provided (used) by operating activities | | |
| Operating income | \$ 25,694,977 | \$ 55,904,417 |
| Adjustments to reconcile operating income (loss) to net cash from operating activities | | |
| (Increase) decrease in accounts receivable | \$ (1,663,444) | \$ 828,103 |
| (Increase) decrease in accounts payable | 6,874,259 | (7,942,216) |
| (Increase) decrease in deferred revenue | 2,095,390 | 3,486,352 |
| Total adjustments | \$ 7,306,205 | \$ (3,627,761) |
| Net cash from (used for) operating activities | \$ 33,001,182 | \$ 52,276,656 |

Local Education Plan — Comparative Statement of Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------|-----------------------|----------------------|
| Assets | | |
| Cash | \$ 115,291,447 | \$ 79,679,296 |
| Insurance accounts receivable | 814 | 812 |
| Accounts receivable | 1,713,263 | 799,344 |
| Total assets | \$ 117,005,524 | \$ 80,479,452 |
| Liabilities | | |
| Accrued liabilities | \$ 27,355,000 | \$ 22,125,000 |
| Accounts payable | 14,324 | 1,153 |
| Deferred revenue | 1,848,931 | 1,554,146 |
| Total liabilities | \$ 29,218,255 | \$ 23,680,299 |
| Net assets | | |
| Unrestricted | \$ 87,787,269 | \$ 56,799,153 |
| Total net assets | \$ 87,787,269 | \$ 56,799,153 |

Local Education Plan — Comparative Statement of Revenues, Expenses and Changes in Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------------|-----------------------|-----------------------|
| Operating revenues | | |
| Premiums | \$ 356,033,005 | \$ 321,735,434 |
| Other | 108 | — |
| Insurance forfeitures | 337 | 21,035 |
| Total operating revenues | \$ 356,033,450 | \$ 321,756,469 |
| Operating expenses | | |
| Benefits/claims | \$ 323,941,437 | \$ 276,353,233 |
| Less: insurance recoveries | (4,608,136) | (3,912,485) |
| Administrative services | 1,326,191 | 1,241,144 |
| Contract services | 20,258,159 | 22,529,779 |
| Total operating expenses | \$ 340,917,651 | \$ 296,211,671 |
| Operating income | \$ 15,115,799 | \$ 25,544,798 |
| Non-operating revenues | | |
| Interest income | \$ 3,929,249 | \$ 1,296,882 |
| Total non-operating revenues | \$ 3,929,249 | \$ 1,296,882 |
| Income before transfers | \$ 19,045,048 | \$ 26,841,680 |
| Transfers from general fund | 11,943,068 | 9,869,564 |
| Change in net assets | \$ 30,988,116 | \$ 36,711,244 |
| Net assets, July 1 | 56,799,153 | 20,087,909 |
| Net assets, June 30 | \$ 87,787,269 | \$ 56,799,153 |

Local Education Plan — Comparative Statement of Cash Flows

| | 30-JUN-06 | 30-JUN-05 |
|---|-----------------------|----------------------|
| Cash flows from operating activities | | |
| Receipts from customers and users | \$ 357,052,503 | \$ 324,092,468 |
| Payments to suppliers | (335,986,478) | (300,605,434) |
| Payments for interfund services used | (1,326,191) | (1,241,144) |
| Net cash from (used for) operating activities | \$ 19,739,834 | \$ 22,245,890 |
| Cash flows from noncapital financing activities | | |
| Transfers in | \$ 11,943,068 | \$ 9,869,564 |
| Net cash from noncapital financing activities | \$ 11,943,068 | \$ 9,869,564 |
| Cash flows from investing activities | | |
| Interest received | \$ 3,929,249 | \$ 1,296,882 |
| Net cash from investing activities | \$ 3,929,249 | \$ 1,296,882 |
| Net increase (decrease) in cash and cash equivalents | \$ 35,612,151 | \$ 33,412,336 |
| Cash and cash equivalents, July 1 | 79,679,296 | 46,266,960 |
| Cash and cash equivalents, June 30 | \$ 115,291,447 | \$ 79,679,296 |
| Reconciliation of operating income to net cash provided (used) by operating activities | | |
| Operating income | \$ 15,115,799 | \$ 25,544,798 |
| Adjustments to reconcile operating income (loss) to net cash from operating activities | | |
| (Increase) decrease in accounts receivable | \$ (913,921) | \$ 643,732 |
| (Increase) decrease in accounts payable | 5,243,171 | (4,252,582) |
| (Increase) decrease in deferred revenue | 294,785 | 309,942 |
| Total adjustments | \$ 4,624,035 | \$ (3,298,908) |
| Net cash from (used for) operating activities | \$ 19,739,834 | \$ 22,245,890 |

Local Education Plan — Required Supplementary Information

The table below illustrates how the local education group insurance fund's earned revenues and investment income compare to related costs of loss and other expenses assumed by the local education group insurance fund for each of the last ten years. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's earned contribution revenues and investment revenues. (2) This line shows each fiscal year's other operating costs of the fund including overhead and claims expense not allocable to individual claims. (3) This line shows the fund's incurred claims and allocated claim adjustment expenses (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called policy year); some of these amounts are unavailable. (4) This section shows the cumulative amounts paid as of the end of successive years for each

policy year; some of these amounts are unavailable. (5) This section shows how each policy year's incurred claims increased or decreased as of the end of successive years; some of these amounts are unavailable. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known. (6) This line compares the latest reestimated incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature policy years. The columns of the table show data for successive fiscal and policy years.

Ten-Year Claims Development Information (expressed in thousands)

| | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|--------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| (1) Required contribution and investment revenue earned (fiscal year) | 95,185 | 109,968 | 123,419 | 126,918 | 166,476 | 203,669 | 250,090 | 287,814 | 323,053 | 359,963 |
| (2) Unallocated expenses (fiscal year) | 3,768 | 5,193 | 6,685 | 13,261 | 15,961 | 19,380 | 21,271 | 23,168 | 23,771 | 21,584 |
| (3) Estimated claims and expenses, end of policy year, net incurred | * | * | * | 141,005 | 185,219 | 210,650 | 248,618 | 263,345 | 296,509 | * |
| (4) Net paid (cumulative) as of: | | | | | | | | | | |
| End of policy year | * | * | * | 124,084 | 162,993 | 189,585 | 223,756 | 238,934 | 268,863 | * |
| One year later | * | * | * | 139,458 | 182,699 | 211,337 | 247,014 | 263,694 | * | |
| Two years later | * | * | * | 139,349 | 182,569 | 211,053 | 246,969 | * | | |
| Three years later | * | * | * | 139,340 | 182,461 | 211,041 | * | | | |
| Four years later | * | * | * | 139,366 | 182,454 | * | | | | |
| Five years later | * | * | * | 139,320 | * | | | | | |
| Six years later | * | * | * | * | | | | | | |
| Seven years later | * | * | * | | | | | | | |
| Eight years later | * | * | | | | | | | | |
| Nine years later | * | | | | | | | | | |
| (5) Reestimated net incurred claims and expenses: | | | | | | | | | | |
| End of policy year | * | * | * | 141,005 | 185,219 | 210,650 | 248,618 | 263,345 | 296,509 | * |
| One year later | * | * | * | 139,401 | 182,581 | 211,199 | 247,111 | 263,738 | * | |
| Two years later | * | * | * | 139,357 | 182,441 | 211,044 | 246,949 | * | | |
| Three years later | * | * | * | 139,361 | 182,455 | 210,981 | * | | | |
| Four years later | * | * | * | 139,365 | 182,449 | * | | | | |
| Five years later | * | * | * | 139,315 | * | | | | | |
| Six years later | * | * | * | * | | | | | | |
| Seven years later | * | * | * | | | | | | | |
| Eight years later | * | * | | | | | | | | |
| Nine years later | * | | | | | | | | | |
| (6) Increase (decrease) in estimated net incurred claims and expenses from end of policy year | 0 | 0 | 0 | (1,690) | (2,770) | 331 | (1,669) | 393 | 0 | * |

* Data not available

Local Government Plan — Comparative Statement of Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------|----------------------|----------------------|
| Assets | | |
| Cash | \$ 19,029,293 | \$ 15,479,837 |
| Insurance accounts receivable | 415 | — |
| Accounts receivable | 578,720 | 257,041 |
| Total assets | \$ 19,608,428 | \$ 15,736,878 |
| Liabilities | | |
| Accrued liabilities | \$ 6,819,000 | \$ 6,865,150 |
| Accounts payable | 16,307 | — |
| Deferred revenue | 249,087 | 198,468 |
| Total liabilities | \$ 7,084,394 | \$ 7,063,618 |
| Net assets | | |
| Unrestricted | \$ 12,524,034 | \$ 8,673,260 |
| Total net assets | \$ 12,524,034 | \$ 8,673,260 |

Local Government Plan — Comparative Statement of Revenues, Expenses and Changes in Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------------|----------------------|-----------------------|
| Operating revenues | | |
| Premiums | \$ 96,109,973 | \$ 103,295,975 |
| Insurance forfeitures | 834 | 1,027 |
| Total operating revenues | \$ 96,110,807 | \$ 103,297,002 |
| Operating expenses | | |
| Benefits/claims | \$ 89,517,673 | \$ 84,909,642 |
| Less: insurance recoveries | (1,492,076) | (2,478,348) |
| Administrative services | 432,415 | 459,476 |
| Contract services | 4,605,442 | 6,191,012 |
| Total operating expenses | \$ 93,063,454 | \$ 89,081,782 |
| Operating Income | \$ 3,047,353 | \$ 14,215,220 |
| Non-operating revenues | | |
| Interest income | \$ 803,421 | \$ 224,530 |
| Total non-operating revenues | \$ 803,421 | \$ 224,530 |
| Change in net assets | \$ 3,850,774 | \$ 14,439,750 |
| Net assets, July 1 | 8,673,260 | (5,766,490) |
| Net assets, June 30 | \$ 12,524,034 | \$ 8,673,260 |

Local Government Plan — Comparative Statement of Cash Flows

| | 30-JUN-06 | 30-JUN-05 |
|---|----------------------|----------------------|
| Cash flows from operating activities | | |
| Receipts from customers and users | \$ 96,302,417 | \$ 104,072,199 |
| Payments to suppliers | (93,123,967) | (90,985,436) |
| Payments for interfund services used | (432,415) | (459,476) |
| Net cash from (used for) operating activities | \$ 2,746,035 | \$ 12,627,287 |
| Cash flows from investing activities | | |
| Interest received | \$ 803,421 | \$ 224,530 |
| Net cash from investing activities | \$ 803,421 | \$ 224,530 |
| Net increase (decrease) in cash and cash equivalents | \$ 3,549,456 | \$ 12,851,817 |
| Cash and cash equivalents, July 1 | 15,479,837 | 2,628,020 |
| Cash and cash equivalents, June 30 | \$ 19,029,293 | \$ 15,479,837 |
| Reconciliation of operating income to net cash provided (used) by operating activities | | |
| Operating income | \$ 3,047,353 | \$ 14,215,220 |
| Adjustments to reconcile operating income (loss) to net cash from operating activities | | |
| (Increase) decrease in accounts receivable | \$ (322,094) | \$ 246,596 |
| (Increase) decrease in accounts payable | (29,843) | (1,920,454) |
| (Increase) decrease in deferred revenue | 50,619 | 85,925 |
| Total adjustments | \$ (301,318) | \$ (1,587,933) |
| Net cash from (used for) operating activities | \$ 2,746,035 | \$ 12,627,287 |

Local Government Plan — Required Supplementary Information

The table below illustrates how the local government group insurance fund's earned revenues and investment income compare to related costs of loss and other expenses assumed by the local government group insurance fund for each of the last ten years. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's earned contribution revenues and investment revenues. (2) This line shows each fiscal year's other operating costs of the fund including overhead and claims expense not allocable to individual claims. (3) This line shows the fund's incurred claims and allocated claim adjustment expenses (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called policy year); some of these amounts are unavailable. (4) This section shows the cumulative amounts paid as of the end of successive years for each

policy year; some of these amounts are unavailable. (5) This section shows how each policy year's incurred claims increased or decreased as of the end of successive years; some of these amounts are unavailable. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known. (6) This line compares the latest reestimated incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature policy years. The columns of the table show data for successive fiscal and policy years.

Ten-Year Claims Development Information (expressed in thousands)

| | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|--------|--------|--------|--------|--------|---------|---------|--------|---------|--------|
| (1) Required contribution and investment revenue earned (fiscal year) | 34,944 | 33,846 | 38,187 | 37,728 | 58,593 | 91,297 | 101,219 | 98,302 | 103,521 | 96,914 |
| (2) Unallocated expenses (fiscal year) | 1,184 | 1,335 | 1,732 | 4,251 | 6,315 | 9,396 | 8,576 | 7,194 | 6,651 | 5,038 |
| (3) Estimated claims and expenses, end of policy year, net incurred | * | * | * | 41,871 | 84,018 | 106,617 | 89,217 | 82,822 | 90,559 | * |
| (4) Net paid (cumulative) as of: | | | | | | | | | | |
| End of policy year | * | * | * | 36,846 | 73,936 | 94,889 | 80,295 | 76,196 | 81,924 | * |
| One year later | * | * | * | 41,796 | 83,286 | 104,893 | 87,967 | 82,622 | * | |
| Two years later | * | * | * | 41,778 | 83,197 | 104,751 | 87,804 | * | | |
| Three years later | * | * | * | 41,778 | 83,167 | 104,718 | * | | | |
| Four years later | * | * | * | 41,757 | 83,184 | * | | | | |
| Five years later | * | * | * | 41,757 | * | | | | | |
| Six years later | * | * | * | * | * | | | | | |
| Seven years later | * | * | * | | | | | | | |
| Eight years later | * | * | | | | | | | | |
| Nine years later | * | | | | | | | | | |
| (5) Reestimated net incurred claims and expenses: | | | | | | | | | | |
| End of policy year | * | * | * | 41,871 | 84,018 | 106,617 | 89,217 | 82,822 | 90,559 | * |
| One year later | * | * | * | 41,782 | 83,241 | 104,826 | 87,880 | 82,529 | * | |
| Two years later | * | * | * | 41,778 | 83,183 | 104,729 | 87,792 | * | | |
| Three years later | * | * | * | 41,758 | 83,186 | 104,710 | * | | | |
| Four years later | * | * | * | 41,757 | 83,185 | * | | | | |
| Five years later | * | * | * | 41,757 | * | | | | | |
| Six years later | * | * | * | * | * | | | | | |
| Seven years later | * | * | * | | | | | | | |
| Eight years later | * | * | | | | | | | | |
| Nine years later | * | | | | | | | | | |
| (6) Increase (decrease) in estimated net incurred claims and expenses from end of policy year | 0 | 0 | 0 | (114) | (833) | (1,907) | (1,425) | (293) | 0 | * |

* Data not available

Medicare Supplement Program— Comparative Statement of Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------|----------------------|----------------------|
| Assets | | |
| Cash | \$ 24,964,145 | \$ 27,645,116 |
| Insurance accounts receivable | 420 | — |
| Accounts receivable | 343,316 | 246,502 |
| Total assets | \$ 25,307,881 | \$ 27,891,618 |
| Liabilities | | |
| Accrued liabilities | \$ 4,791,367 | \$ 5,772,000 |
| Accounts payable | 835 | 162 |
| Deferred revenue | 1,871,499 | 887,428 |
| Total liabilities | \$ 6,663,701 | \$ 6,659,590 |
| Net assets | | |
| Unrestricted | \$ 18,644,180 | \$ 21,232,028 |
| Total net assets | \$ 18,644,180 | \$ 21,232,028 |

Medicare Supplement Program— Comparative Statement of Revenues, Expenses and Changes in Net Assets

| | 30-JUN-06 | 30-JUN-05 |
|-------------------------------------|----------------------|----------------------|
| Operating revenues | | |
| Premiums | \$ 27,371,018 | \$ 37,388,545 |
| Total operating revenues | \$ 27,371,018 | \$ 37,388,545 |
| Operating expenses | | |
| Benefits/claims | \$ 32,599,515 | \$ 39,898,018 |
| Less: insurance recoveries | (1,223,275) | (1,001,377) |
| Administrative services | 337,783 | 631,794 |
| Contract services | 5,182,514 | 5,606,123 |
| Total operating expenses | \$ 36,896,537 | \$ 45,134,558 |
| Operating income (loss) | \$ (9,525,519) | \$ (7,746,013) |
| Non-operating revenues | | |
| Interest income | \$ 1,045,381 | \$ 591,893 |
| Total non-operating revenues | \$ 1,045,381 | \$ 591,893 |
| Income (loss) before transfers | \$ (8,480,138) | \$ (7,154,120) |
| Transfers from general fund | 5,892,290 | 5,802,560 |
| Change in net assets | \$ (2,587,848) | \$ (1,351,560) |
| Net assets, July 1 | 21,232,028 | 22,583,588 |
| Net assets, June 30 | \$ 18,644,180 | \$ 21,232,028 |

Medicare Supplement Program — Comparative Statement of Cash Flows

| | 30-JUN-06 | 30-JUN-05 |
|---|-----------------------|-----------------------|
| Cash flows from operating activities | | |
| Receipts from customers and users | \$ 28,257,854 | \$ 37,710,311 |
| Payments to suppliers | (37,538,713) | (44,078,856) |
| Payments for interfund services used | (337,783) | (631,794) |
| Net cash from (used for) operating activities | \$ (9,618,642) | \$ (7,000,339) |
| Cash flows from noncapital financing activities | | |
| Transfers in | \$ 5,892,290 | \$ 5,802,560 |
| Net cash from noncapital financing activities | \$ 5,892,290 | \$ 5,802,560 |
| Cash flows from investing activities | | |
| Interest received | \$ 1,045,381 | \$ 591,893 |
| Net cash from investing activities | \$ 1,045,381 | \$ 591,893 |
| Net increase (decrease) in cash and cash equivalents | \$ (2,680,971) | \$ (605,886) |
| Cash and cash equivalents, July 1 | 27,645,116 | 28,251,002 |
| Cash and cash equivalents, June 30 | \$ 24,964,145 | \$ 27,645,116 |
| Reconciliation of operating income to net cash provided (used) by operating activities | | |
| Operating income (loss) | \$ (9,525,519) | \$ (7,746,013) |
| Adjustments to reconcile operating income (loss) to net cash from operating activities | | |
| (Increase) decrease in accounts receivable | \$ (97,234) | \$ 216,974 |
| (Increase) decrease in accounts payable | (979,960) | 423,908 |
| (Increase) decrease in deferred revenue | 984,071 | 104,792 |
| Total adjustments | \$ (93,123) | \$ 745,674 |
| Net cash from (used for) operating activities | \$ (9,618,642) | \$ (7,000,339) |

Medicare Supplement Program — Required Supplementary Information

The table below illustrates how the medicare supplement insurance fund's earned revenues and investment income compare to related costs of loss and other expenses assumed by the medicare supplement insurance fund for the last ten years as previous year's information becomes available. As of June 30, 2005, only 54 months of data were available. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's or period's earned contribution revenues and investment revenues. (2) This line shows each fiscal year's or period's other operating costs of the fund including overhead and claims expense not allocable to individual claims. (3) This line shows the fund's incurred claims and allocated claim adjustment expenses (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called policy year); some of these amounts are unavailable. (4) This section shows the cumula-

tive amounts paid as of the end of successive years for each policy year; some of these amounts are unavailable. (5) This section shows how each policy year's incurred claims increased or decreased as of the end of successive years; some of these amounts are unavailable. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known. (6) This line compares the latest reestimated incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature policy years. The columns of the table show data for successive fiscal and policy years.

Ten-Year Claims Development Information (expressed in thousands)

| | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|------|------|------|------|---------|--------|--------|--------|--------|--------|
| (1) Required contribution and investment revenue earned (fiscal year) | — | — | — | — | 20,145* | 44,015 | 34,762 | 37,094 | 37,980 | 28,416 |
| (2) Unallocated expenses (fiscal year) | — | — | — | — | 2,375* | 4,887 | 5,433 | 5,736 | 6,238 | 5,520 |
| (3) Estimated claims and expenses, end of policy year, net incurred | — | — | — | — | 28,163 | 32,387 | 36,105 | 39,074 | 42,756 | ** |
| (4) Net paid (cumulative) as of: | | | | | | | | | | |
| End of policy year | — | — | — | — | 23,657 | 27,205 | 31,050 | 33,604 | 36,770 | ** |
| One year later | — | — | — | — | 28,536 | 31,875 | 35,943 | 38,790 | ** | |
| Two years later | — | — | — | — | 28,662 | 31,888 | 35,993 | ** | | |
| Three years later | — | — | — | — | 28,658 | 31,878 | ** | | | |
| Four years later | — | — | — | — | 28,658 | ** | | | | |
| Five years later | — | — | — | — | ** | | | | | |
| Six years later | — | — | — | — | | | | | | |
| Seven years later | — | — | — | — | | | | | | |
| Eight years later | — | — | — | — | | | | | | |
| Nine years later | — | — | — | — | | | | | | |
| (5) Reestimated net incurred claims and expenses: | | | | | | | | | | |
| End of policy year | — | — | — | — | 28,163 | 32,387 | 36,105 | 39,074 | 42,756 | ** |
| One year later | — | — | — | — | 28,623 | 31,890 | 35,984 | 38,809 | ** | |
| Two years later | — | — | — | — | 28,659 | 31,879 | 35,993 | ** | | |
| Three years later | — | — | — | — | 28,658 | 31,874 | ** | | | |
| Four years later | — | — | — | — | 28,657 | ** | | | | |
| Five years later | — | — | — | — | ** | | | | | |
| Six years later | — | — | — | — | | | | | | |
| Seven years later | — | — | — | — | | | | | | |
| Eight years later | — | — | — | — | | | | | | |
| Nine years later | — | — | — | — | | | | | | |
| (6) Increase (decrease) in estimated net incurred claims and expenses from end of policy year | — | — | — | — | 494 | (513) | (112) | (265) | 0 | ** |

— Coverage was fully insured through December 2000

* Amounts only represent a 6-month fiscal period

** Data not available